

## **Implications Increase of Protectionism Between USA and China for International Business**

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*Abstract* - The main aim of this paper is presentation the implications increase of protectionism between the United States and China on international business. The main objective of the research task is to give a comprehensive analysis of current trends in foreign trade theory and policy and in particularly the models of foreign trade policy, trade interests indicated by export orientation and import sensitivity, protectionist pressures in different political system, the level of protectionist pressures, new tendencies in international business, reasons for the USA to implement tariff sanctions. China will be significantly hurt by tariff trade war in all indicators, including welfare, gross domestic product (GDP), manufacturing employment and trade. However, it is pointed out that although there will be definite impacts on China, the costs should be maintainable and will not severely damage the Chinese economy. In regard to the United States, the simulation produced results that described, the US will gain on welfare, GDP and non-manufacturing production, but hurt employment and trade.

*Key-Words*:- USA, China, protectionism, international business, supply chains, trade war.

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## 1 Introduction

Both structural and micro-political economy analyses of foreign trade policy have missed the impact of changing ideas about protectionism and relatively unchanging institutions designed to handle domestic producer complaints. The political consensus on the supply of the trade policy and protectionism has changed over the time. During economic depression protectionism played important roles in the politics of political parties and increased the importance of bilateral agreements and regional agreements. This point of view is very important for the theory and practice of the contemporary international business also between USA and China.

The necessity for companies to organize their supply chains across different countries has led to a demand for the regional agreements that cover more than preferential tariffs. The harmonization of standards and rules on investment, intellectual property and services has become a standard part of new trade agreements. The differences among companies which are involved in trade are also important for the future development. The concept that arises from the trade is that even if many companies are indirectly involved into the trade-related activities, only relatively few of them are exporting or importing. Accordingly, these companies tend to be larger and more productive than others. Such companies also have a role in technology advancement and the diffusion of know-how through supply chains. It should be emphasised also that free trade in itself is not responsible for economic growth, but more significant are the determining macroeconomic stability and increasing investment.

The international trade in the XXI century has been strongly affected by the force of the domestic interests like in the USA under President Donald Trump's administration with the principle *America First*. The changes are visible in the growing importance of international trade to national economies and domestic groups within those economies, in the closer linkages between trade and other international issues. Realistic point of view is the essential trends in the global trade regime during this time. The growing interdependence has led to increased competitiveness and greater inclinations to resort to strategic trade policy.

## 2 Research and Methodology

The primary research objective of this paper is to conduct a comprehensive analysis of the potential implications of the United States and China

increasing their trade barriers. China will be significantly hurt by a tariff trade war in all indicators, including welfare, GDP, manufacturing employment, and trade. However, it has been pointed out that, although China will be significantly affected, the costs should be sustainable and not severely damage the Chinese economy. As for the United States, the simulation results indicate that there will be welfare, GDP and non-manufacturing production gains, but employment and trade losses.

Both quantitative and qualitative research methods were used for analytical purposes. The main research method applied in this analysis was a method of scientific study that breaks down a whole (of individual items, their sets, and various phenomena) by means of logical abstraction. The analogy (comparative) method, which consists in finding similarities and differences between the items under study, the documentation method, and various statistical methods were also applied, as were other descriptive statistics and forecasting methods. Finally, deductive and inductive forecasting were employed.

## 3 Results and Discussion

The importance and innovativeness of this research lies in the fact that it reveals the potential implications of the increasing protectionism between the United States and China. First, it emphasizes the importance of "factor specificity" (a new theoretical term) in the demand for trade policy. Some factors have retained their existing uses. Factor returns are therefore not equalized throughout a region's economy, but are industry specific. Trade policy coalitions should be formed along the lines of exporting versus import-competing industries. Understanding the choice between liberal and protectionist trade policies is therefore crucial at the theoretical level.

What is at issue is how to recognize the type of power or rule at play. First, the level of resources that can be achieved by a given government has to be investigated. How much more income an authoritarian government can generate through protectionism depends on how corrupt it is compared to its democratic trading partner(s). It will also appropriate some part of that income. Secondly, any government, whatever its political system or power structure, is susceptible to pressure from special interest groups, including regulated labor. No government, no matter how authoritarian, can subordinate these groups unless it transfers some of the income generated by its protectionist policies to them.

The close relationship between democracy and economic growth is worth noting. Examples of open societies stimulating economic growth are not hard to find. This is especially true in the case of highly developed and urbanized countries. Pressure groups potentially have more influence over the government in a developed democracy. Research shows that trade unions help accelerate economic reforms. The benefits of liberalizing international trade are greater when the protected sectors of the economy are unionized. The growth of import abilities leads to a decrease in wage pressures. If the trade unions accept this, then labor can be more efficiently allocated. This is true in the case of both active and passive trade unions, although active trade unions obviously achieve better results.

Increasing interdependence has led to greater competitiveness and more inducements to resort to strategic trade policy. Trade policy assumes further significance in the economic battle of valiant liberal reformers in their fight against self-dealing rent seekers profiting from inconsistencies in the transition economy. Many of the client policies that shelter rent seekers are impossible to maintain in the face of international competition. On the other hand, high tariff walls, export licensing, and artificial exchange rates provide numerous sources of rents for businesspeople out to promote their own loyalties.

The reduction or elimination of trade restrictions significantly stimulates world trade and conversely, foreign trade is an important factor driving the economic growth of individual countries. However, it should be stressed that free trade is not the sole contributing factor to economic growth; macroeconomic stability and investment are more significant.

It has to be stressed that if unemployment is increasing and/or inequality widening while global supply chains are expanding and multiplying, and if most voters attribute the former to the latter, then governments may well refrain from pursuing further international trade liberalization and might even find protectionism alluring. Another possibility would be for governments to use more intensively public policies for protectionist purposes. As for trade negotiations, focusing exclusively on the increased efficiency resulting from opening up trade is no longer possible. Distribution and labor-market effects also need to be considered and various measures proposed in order to win the electorate over to open trade by bilateral agreement, especially at times when global supply chains are expanding and multiplying.

As global supply chains have expanded and

multiplied, the formulation of new theoretical models of the firm have made it possible to explore the effects that differences in firms have had on the political economy of trade. It has to be stressed that opening up trade has had two opposing effects on domestic firms in the same industry. First, the cost of exporting decreases, which obviously allows more firms to export and increases the sales of established exporters. Secondly, competition increases, which harms domestic firms. Which of these opposing tendencies prevails for an individual firm depends on such characteristics as size. As a result, lobbying competition arises not only between sectors but also within sectors with the inevitable result that there are winners and losers. This might especially be the case when costs are fixed, because barriers to entry are raised, thereby shielding existing producers and exporters from competition.

Current trends in international business and global politics provide evidence that emerging markets have finally made their presence felt on the world economy, bringing new patterns of uneven development, inequality and injustice in their wake. Their newly confident elites, now active on global circuits of trade, investment and finance, and in global governance, appear to have shed their previous roles. It is clear that emerging economies have suffered less severely and recovered more quickly. Moreover, it now seems that the political impact is not so much immediate crisis measures, but significant, long-term and unexpected policy shifts.

### **3. 1 Political Economy Model of Foreign Trade Policy**

Traditionally, political economy models of trade policy have tended to focus on demands for protection, with factor endowments driving political reactions to exposure to international trade. These models simply assumed that adversely affected economic agents would organize and lobby their elected political representatives for protection. The supply side for trade policy was either ignored or underspecified in most models [50].

Some of the reviews of the new model of foreign trade policy theory are interesting insofar as they concern the demand for trade policy in terms of the theoretical importance of factor specificity [2] [26]. Factor specificity refers to the ease with which factors (land, labor, and capital) can move from one sector to another in an economy. The two dominant approaches to explaining the demand side of trade policy used radically different assumptions about the specificity of factors. The Heckscher-Ohlin model, used by Rogowski (1989) in his seminal

contribution *Commerce and Coalitions*, assumes very low-factor specificity [46]. Low factor specificity means that factor returns are equalized throughout a region's economy. Producers should export goods that intensively use their abundant factors and import goods that intensively use their scarce factors, with the result that owners of abundant factors will favor free trade and owners of scarce factors will favor protectionism. Trade policy coalitions will therefore be organized along factor or class lines. The Ricardo-Viner model, per contra, assumes that some factors are stuck in their present uses and that factor returns are therefore not equalized throughout a region's economy, but are industry specific. Trade policy coalitions should form along the lines of exporting versus import-competing industries.

Neither of these models explains how preferences over trade policies are actually translated into political action [2]. In a discussion of the endogenous tariff literature, Nelson (1988) notes that the mobility costs of the specific-factors model may be a result of productivity differentials, labor union activity, or individual preferences for membership in a given geographical area, industry, or firm (i.e. some form of solidarity) [26]. In all of these cases, a link to tariff policy preferences can be derived, "but without additional information on why the specific-factor model is chosen, it does not tell us much about political organization".

Alt et al. (1996) suggest that we can begin to understand this process by assuming that rational individuals make cost/benefit calculations [2]. The Heckscher-Ohlin and Ricardo-Viner models enumerate the benefits that individuals hope to receive, but the costs of collective action also intervene as they organize to achieve those benefits in the political system. Olson (1985) argued that small special-interest groups are easier to organize and more effective in securing economic rents than large groups with diffuse interests [27]. Small groups are better able to control free riders than large groups, and groups with specific or homogenous interests can more easily coordinate and target their activities than groups with diffuse or heterogenous interests [35]. This approach is thought to explain the success of agricultural producer groups in developed countries in organizing for protection [35] as well as the inability of agricultural producer group to organize in developing countries [3] [7] [27][28][49].

However, Nelson (1988) points out that organized interests should not be assumed to be equally responsive to all issues [26]. Institutionalized interaction among actors may help

to explain systematic patterns of action, especially as institutions created for specific historical purposes may outlive those purposes. Alt et al. (1996) suggest that if a particular group has paid the fixed costs of establishing collective action and developed well-worn channels of access to public officials, it may defend its trade policy preferences even when the stakes are low because the marginal costs of action are low [2]. It may be the case that "a much more affected but inchoate group does nothing because the start-up costs of organization are too daunting [35]. Past strength of an organization should therefore be an important intervening variable predicting group action on trade policy. Further, as Nelson (1988) argues, once these institutions exist, supply-side interventions may also affect their usefulness as some are deemed legitimate or illegitimate aggregators of interest [26]. The ways in which economic institutions and political institutions interact must therefore be examined. Most economic models simply assume that a model of the economy is a model of the demand side for trade policy, but Nelson (1988) suggests that we have to elaborate the mechanism by which demand is articulated to the suppliers of trade policy [26]. For a good overview of this argument, especially as it pertains to agriculture [50].

If the political system rewards small sectoral groups, then individuals will decline to incur the costs of organizing large intersectoral coalitions. If the political system rewards large mass movements (i.e. majoritarianism), then individuals will have to incur the costs of organizing large intersectoral coalitions in order to achieve any benefits. The costs of collective action and the nature of political institutions interact with factor specificity. This suggests that Rogowski's (1989) Heckscher-Ohlin framework requires low factor specificity, low collective action costs, and domestic political institutions that favor mass movements [46]. The Ricardo-Viner framework used by the endogenous tariff literature requires specific factors, high collective action costs, and non-majoritarian institutions. The nature and extent of these three variables affects the type of coalitions that form.

In the state as rational dictator model, the state may be seen as either pursuing "good government" goals along a social welfare function or intervening in the economy for its own interests. This model views politicians as offering preferential trade policy to economic actors in exchange for political support [24] [13]. On the other hand, pluralist theory typically views the state as a neutral aggregator of demands from groups in society. The supply side of trade policy is then determined by the balance of

power on any given issue. This is still in the early stages of theoretical development, but is vitally important. Various characteristics of the political system are posited to affect the supply of trade protectionism, such as incentives for politicians to cultivate personal votes, the size of electoral districts, party fragmentation, federal versus unitary structures, presidential versus parliamentary systems, etc. [45] [47] [48].

Understanding the trade policies adopted by different countries is crucial at the theoretical level. A 1984 survey of economists found that one of the few things they agreed on was that, under most conditions, tariffs, and quotas reduce general welfare [10]. The persistence of protectionism in the face of international and academic resistance has led economists to seek explanations. These explanations range from simple ignorance on the part of politicians to the (questionable) rationality of having to protect “infant industries” and the need for developing states to impose “optimal tariff levels”. Scholars have increasingly turned to politics in order to explain apparently irrational policy decisions out of sheer frustration [10]; [25]; [26].

### **3. 2 Protectionist Pressures in Different Political Systems**

It is important to note that trade unions can play very different roles in different political systems. As a rule, their role is smaller in authoritarian systems than it is in democratic systems. The prospects for economic growth are obviously more promising when the trade unions are unable to exert undue protectionist pressure. This line of reasoning justifies the conclusion that authoritarian systems are more conducive to labor market efficiency, and the examples of Chile, South Korea, Singapore and Turkey during the 1970s and early 1980s could be said to bear this out. Many authoritarian regimes persecuted trade unions and restricted basic labor rights during those two decades. However, South Korea, Singapore and Turkey experienced spectacular growth in their processing industries and in the demand for labor throughout that oppressive period. Greater profitability and the increasing demand for labor in the processing industry made the workforce more prosperous. Although similar results were not noted immediately during the authoritarian development phase in Chile, a number of observers are of the opinion that the reforms introduced at that time contributed to the reorganization of the Chilean economy in the 1990s. The application of democratic norms, by contrast, can lead to lower labor productivity. During the period in question, several democratic countries

were obliged to employ trade union members at considerable extra cost.

An alternative viewpoint has it that labor legislation can be applied more effectively in an authoritarian system than it can in a democratic one. Authoritarian regimes often exploit the specific interests of various groups. Few democratic countries have a broad enough consensus to win the support of pressure groups (the urbanized labor market elite included) by means of labor market policy. The major difference between authoritarian and democratic regimes lies in the level of influence that can be exerted on the government and by whom. In a well-functioning democracy, various, often conflicting, viewpoints have to be accommodated and special interest groups constrained. In a dictatorship, by contrast, the government is only concerned to see that these groups do not become too powerful [35].

There are, however, several democracies among both the industrialized and developing countries that have an effective labor market. Moreover, an effective labor market is often a priority in countries moving away from authoritarianism towards democracy.

It is worth considering which of the two viewpoints presented above should be adopted. The Grossman and Helpman model [13] may be of assistance here. This model describes economic development in terms of the urbanized, regulated processing sector, and the rural, unregulated agricultural sector. Labor protection legislation, especially minimum wage laws, is obviously designed to benefit the regulated sector.

Not surprisingly, the regulated labor force, and employers, demand that the government formulate economic policies favorable to them. Workers demand high minimum wages and their employers demand high profits. Both groups demand that restrictions be placed on the openness of the economy. In a closed economy, higher minimum wages and profits are usually correlated with higher prices for domestic consumers, as imported substitutes are not readily available. Protection can therefore generate income, which can then be divided among workers and their employers in the regulated sector, although the government sometimes appropriates part of it [5].

Governments have to consider several factors when implementing economic policy. Firstly, they have to determine their share of the anticipated benefits. This explains the importance of investment and economic growth, and of assessing the likelihood of maintaining power. Secondly, the level of support that can be expected from each of

the pressure groups capable of influencing the situation needs to be specified. The position and importance of each group for the development of political processes has to be carefully weighed [60]. For example, if the regulated labor market is divided and politically weak, then only employers might have any real say in the political process. The opposite can also occur; a well organized labor force can play a major role in mobilizing voters.

How can we recognize the type of power? Firstly, the benefits the government has set out to deliver need to be identified. Whether an authoritarian government can generate more income than a democratic one through protectionism largely depends on how corrupt it is. The government can also be counted on to appropriate part of that income. Secondly, the government may be influenced by various pressure groups. When an authoritarian government attempts to subordinate special-interest pressure groups, including the regulated labor sector, it inevitably transfers some of the income generated through protection to them.

### 3. 3 Level of Protectionist Pressures

The above arguments show that policy is shaped by political factors (including the type of government and its obligations towards employers and employees), and by economic factors (wages, prices, the structure of production and consumption). In light of the present discussion, we can present two equations: one pertaining to the level of protection, and the other to the national economy and deformation of wages.

$$(1) \quad \pi = f(e, l, k, R)$$

$$(2) \quad \varphi = f_1(\pi, e, l, k, R).$$

The level of protection ( $\pi$ ) is a function of the economic parameters ( $e$ ), the relative political importance of the urbanized labor force and its employers ( $l$  and  $k$ , respectively), and on the type of government ( $R$ ). Wage distortions are a function of  $\pi$  and of  $e$ ,  $l$ ,  $k$  and  $R$ . In the case of a small economy, economic parameters that can influence  $\pi$  and  $\varphi$  include the flexibility of consumer and producer prices and demand, wages, the demand for labor, and the price of goods on the international market.

By definition, the growth of  $\pi$  is dependent on  $l$  and  $k$ . When interest groups become stronger, there is greater pressure to raise income through protectionism. The influence of  $R$  (the degree of authoritarianism) on  $\pi$  (the level of protectionism) depends on whether  $\pi$  depends on the nature and extent of democratization. It is also thought that wage distortion increases with  $\pi$  and  $l$ , and decreases with  $k$ . So long as the extra income is obtained from

trade protection, it can be distributed among the urbanized labor force. However, one major problem facing the urbanized labor force, as a special interest group gaining in strength, is that any potential gains in the division of income may be offset by the political clout of its employers with the result that it will actually receive a smaller share in regulated sectors of the economy [9].

It is obviously easier for wealthy societies to choose democracy than it is for poor ones. Moreover, as wealthy societies also tend to be more open, the direction of causation may run from a society's level of openness to its political system, and not vice versa, as suggested earlier. Research also shows that educational level plays an important role in this respect. Countries with higher educational levels tend to be more open.

The above considerations warrant the conclusion that authoritarian systems tend to apply protectionism more broadly than democratic systems, and that trade restrictions are correlated with significant wage distortions. This can be justified on the basis of the observable situation in a number of countries.

Freedom of association is a sign of good management and a precondition for development. Authoritarian governments, however, do not respect freedom of association. To do so would run counter to their policies of restricting trade and distorting the labor market. That is not to say, however, that improper or ineffective labor market policies are the preserve of authoritarian regimes or that authoritarianism automatically generates this kind of policy. There are any number of examples of authoritarian countries which do not pursue such policies. The works of such authors as Fields or Freeman show that it is not necessary to keep workers down to achieve the desired level of economic growth.

Finally, it should be noted that there is a close relationship between democracy and economic growth. Indeed, there are well-documented cases of open societies stimulating economic growth. This is especially true in the case of highly developed and urbanized countries. Pressure groups have greater scope for action in countries with a developed democracy. Research shows that trade unions can accelerate economic reform. The benefits of liberalizing international trade are greater when the protected sectors of the economy are unionized. Increased import opportunities reduce wage pressures. If the trade unions accept this, then labor can be more efficiency allocated. This is true both in the case of active and passive trade unions, although the former obviously achieve better results.

Trade unions active on urbanized labor markets significantly influenced government decision-making during the WTO multilateral trade negotiations. This was especially evident during the negotiations on lowering customs duties and non-tariff protection measures in the steel, shipbuilding, textile and clothing industries, and in coal mining. The trade unions were particularly strong in “sensitive” industries, which were under special trade protection.

### **3. 4 New Tendencies in International Business**

Countries and producers increasingly specialize in certain stages of production depending on comparative advantage [20][25]. This is an important development for foreign trade policy. It should also be emphasized that transport and energy costs partly explain why supply chains are still mostly regional. Krugman (1991) incorporates increasing returns, together with capital and labor migration and transport costs, into a single model. Krugman’s (1991) model has become a workhorse of economic geography and international trade. It is too complex to explain here, but the reasons for that complexity are clear – when everything becomes “endogenous”, small variations in a single factor can have huge knock-on effects. For example, in order to minimize transport costs, firms want to be near actual and potential customers, consumers want to be close to goods and services providers, and workers want to be close to where they can find work. There are therefore multiple equilibria, and there can be a tipping point where the location decisions of a single firm, customer and/or worker can snowball. A related trend is a new form of regionalism that is sometimes referred as integration process development [4].

It needs to be emphasized that openness to trade with China is associated with higher incomes and growth and that there need to be new approaches to trade in light of the forces that are currently reshaping international business. A major factor in this has been the remarkable transformation of China, as market reforms have opened up its economy to foreign trade and investment, and unleashed unprecedented economic growth. This is ongoing and has only witnessed minor slowdowns. Under the conditions in which the global economy and global trade are developing, the People’s Republic of China appears to be a production superpower that can change world trade and influence the rise of global supply chains. The country has a comparative advantage in many areas and is moving to specialize in electronics and increasingly in services.

The major trend in international trade is the rise of several emerging economies and the associated increase in their shares in world trade [25]. This applies especially to China, but India and Brazil have also altered the balance of power in the multilateral trading system [25]. Between 1980 and 2011, for example, China’s share in world merchandise exports and imports increased tenfold, making the country the largest exporter of the world [25] [22].

The industrialization and spectacular growth of emerging economies, together with the rapid expansion of trade in services and of FDI, are inextricably linked to the next intensive phase of production growth. The focus here will be on how the rise of global supply chains can impact the political economy of trade and on how to induce countries to work together on bilateral trade policies [16]. That participation in global supply chains tends to strengthen anti-protectionist forces has both theoretical and empirical support [16]. The main impact has been unilateral tariff reductions (mostly among developing countries), and the proliferation of preferential trade agreements (PTAs) and bilateral investment treaties [20][16]. A considerable amount of trade opening has thus taken place outside the WTO.

The internationalization of supply chains has proven vital for the rapid economic development and industrialization of developing countries. Before the emergence of supply chains – and the information and communications technology (ICT) revolution that underpinned them – industrialization involved building a strong industrial base, often behind a wall of tariffs and other protective measures (NTMs)[17]. The unbundling of global production has enabled countries to industrialize by joining international supply chains [16]. This process has also changed the political economy of trade policy, and created a strong incentive to undertake unilateral tariff reductions in many developing countries.

### **3. 5 The Structure of Political System**

The US claims that Chinese state-owned enterprises are typical by-products of a communist planned economy, and that crony capitalist princelings derive the greatest benefits from most of their initiatives, including the Belt and Road Initiative [29][40][44][39] and Made in China 2025. The US, Japan, Canada, Mexico, and the EU do not recognize China as a market economy, alleging market distortions. Economist Irwin Stelzer states that China’s centrally directed economy, designed to preserve communist party control of the nation’s politics and its economy, is relevant to US trade

policy. Aaron Friedberg, a political scientist and former White House national security officer, has also said the communist Chinese regime has considerably expanded its use of state-directed, market-distorting, mercantilist policies since 2008 [33]. The 2018 Congressional hearing “U.S. Tools to Address Chinese Market Distortions” discussed how “the Party leads everything” doctrine makes it difficult to apply trading rules to the Chinese economy and results in many US businesses bowing to pressure, even though their decisions risk jeopardizing the future of their companies and the US economy as a whole. The Chinese Communist Party is fundamentally opposed to free-market capitalism and fair competition. The US cites this as the root cause of US–China economic tensions [29].

China is a totalitarian mercantilist regime in a state of an economic war with the West. Trade war by China against the United States has been going on for years” (Fig. 1). China declared trade war on the US 18 years ago in control and command economies like China, a telephone call in the middle of the night from a monopoly commissar is all that it takes to get a business to do something (Fig. 1). China is totalitarian regime and states China's unfair trade

Fig. 1: The rapidly increasing US trade imbalance with China.

policies are kind of economic aggression and a direct result of its autocracy. The economic security is the national security and discusses trade in a broader geopolitical arena.

China counterclaims that the US government has long practiced unilateralism, protectionism and economic hegemony, made false accusations against many countries and regions, particularly China, intimidated other countries through economic sanctions such as tariffs, and attempted to impose its own interests on China through duress.

China has stolen US intellectual property and bullied its way into acquiring critical US advances in technology. Tariffs are an important tool to put an end to trade practices that are destroying American jobs and driving down American wages.

Many countries and companies have accused Chinese spies and hackers of stealing technological and scientific secrets by installing malware and infiltrating industries, institutions, and universities. China has also been accused of stealing foreign designs, flouting product copyrights and implementing a two-tier patent system that discriminates against foreign companies with

unreasonably longer times. The Chinese intelligence service was accused of assisting Chinese companies by stealing company secrets.

Chinese hackers have consistently stolen trade secrets from US defense contractors. Chinese cybertheft of intellectual property is the greatest transfer of wealth in history. Chinese spies have gone after private defense contractors and subcontractors, national laboratories, public research universities, think tanks, and even the US government. Chinese agents have gone after crucial US defense assets, such as the F-35 Lightning, the Aegis Combat System, and the Patriot Missile System. They have illegally appropriated unmanned underwater vehicles and thermal imaging cameras, and have stolen documents related to the B52 Bomber, the Delta IV Rocket, the F15 Fighter, and even the Space Shuttle. The US opened a formal investigation into attacks on the intellectual property of the US and its allies, which was costing the US alone an estimated \$225–600 billion a year.

### **3. 6 Reasons for the USA to Impose Tariff Sanctions**

China and the United States are engaged in a trade war, with each disputing the tariffs the other imposes on its goods. These economic disputes began before China joined the World Trade Organization (WTO). In April 2018, the United States filed a request for consultation to the WTO in regard to concerns that China was violating intellectual property rights.

By adding various tariffs, the US administration is partly relying on Section 301 of the Trade Act of 1974 to prevent what it calls unfair trade practices and theft of intellectual property. This gives the president the authority to unilaterally impose fines or other penalties on a trading partner if it is deemed to be unfairly harming US business interests, especially if it is deemed to have violated international trade agreements. In August 2017, the US opened a formal investigation into attacks on the intellectual property of the US and its allies.

The result is that the US believes Chinese laws undermine intellectual property rights by forcing foreign companies to engage in joint ventures with Chinese companies, which then gives these companies access to foreign technologies and permission to appropriate, copy and use them. The US has also raised concerns that China refuses to recognize legitimate patents and copyrights, discriminates against foreign imported



technology, and has instituted numerous non-tariff barriers to effectively insulate sectors of the Chinese economy from international competition. Thus, the trade war is seen as largely focused on intellectual property, especially in the area of science and technology.

China's technological progress is coming from businesspeople who are benefitting from the vast sums their government invests in basic science. The Chinese education system privileges excellence and focuses on science and technology. That's where their leadership in some technologies is coming from, not from taking a stake in some US company. China declared that its attitude toward the protection of intellectual property rights is clear and firm, and it has continuously strengthened protection at the legislative, law enforcement, and judicial levels, with remarkable results.

The US claims that China requires technology transfer through a Foreign Direct Investment (FDI) regime and often requires joint ventures: in many cases, technology transfers are effectively required by China's FDI regime, which closes off important sectors of the economy to foreign firms. In order to gain access to these sectors, China forces foreign companies to enter into joint ventures with Chinese entities with which they have no connection.

A number of experts have focused on what they claim is China's "theft" of intellectual property, saying that China forces any US company wanting to do business there to transfer confidential technology and trade secrets before it will grant access to its market. Although that kind of transfer is in breach of WTO rules, the negotiations are usually conducted in secret to avoid penalties. The Commission on the Theft of American Intellectual Property states claims that agreeing to manufacture in China is tantamount to agreeing to transfer technology or have it stolen. The Commission recommended a response based on "strength and leverage".

In 2018, the American Chamber of Commerce in China learned that over half its members cited "leakage of intellectual property" as an important concern when doing business there. Similarly, the EU Chamber of Commerce has also complained that European companies wanting access to the Chinese market often have to agree to transfer vital technology. China claims that technical, economic, and trade cooperation between Chinese and foreign enterprises is completely based on contracts voluntarily entered into, that both

companies obtain practical benefits, and that over the years, US companies in China have not only benefitted enormously through technology transfer and licensing, but are the biggest beneficiaries of technical cooperation.

In June 2016, as presidential candidate, Donald Trump vowed to cancel international trade deals and go on an offensive against Chinese economic practices, describing his promise as a reaction against "a leadership class that worships globalism". Less than a year after he took office, the United States, European Union and Japan, agreed to work within the World Trade Organization (WTO) and other multilateral groups to eliminate unfair subsidies by countries, which create noncompetitive conditions through state-owned enterprises, "forced" technology transfers and local content requirements.

In April 2018, President Donald Trump denied that the dispute was actually a trade war, saying that war was lost many years ago by the foolish, or incompetent, people who represented the US. He added also that in the 2018 year USA have a trade deficit of \$500 billion a year, with intellectual property (IP) theft of another \$300 billion (Fig. 2) and that US cannot let this continue.

Fig. 2: US Trade Representative.

In January 2018, President Donald Trump underlined he wanted the United States to have a good relationship with China, but insisted that it treat the United States fairly. In his State of the Union Address a few weeks later, mentioned that America has also finally turned the page on decades of unfair trade deals that sacrificed prosperity and shipped away companies, jobs, and Nation's wealth. The era of economic surrender is over. From this time America expect trading relationships to be fair and to be reciprocal. United States will work to fix bad trade deals and negotiate new ones and US government will protect American workers and American intellectual property, through strong enforcement of US trade rules.

A number of government and industry experts have offered their own rationales as to why tariffs are, or are not, appropriate. John Ferriola, the CEO and President of Nucor, America's largest steel producer and metal recycler, argued that tariffs were not unfair, but were "simply leveling the playing field". Ferriola went on to explain that most countries, including EU member states, levy VAT rates of at least 25% on US imports. If the US imposed a 25% tariff, it would therefore be doing no

more than treating these countries exactly as they treat the US.

It is claimed that China has instituted an array of non-tariff barriers and that this has shielded critical sectors of the Chinese economy from international competition. China has controlled imports by having different standards for private, foreign companies than for Chinese State Owned companies. Lee G. Branstetter, a professor of economics and public policy at Carnegie Mellon University, has listed some of the ways that China has misappropriated foreign technology. In a report dated March 22, 2018, the US cited numerous instances of forced technology transfer and the failure of companies and the government to protect US intellectual property from infringement or theft. Soon after the report came out, the US announced plans to impose tariffs on up to \$60 billion worth of Chinese exports to the United States and to tighten the rules governing Chinese investment in the United States.

Despite doubts being raised over US strength and leverage, security implications, and China's appalling human rights record, the Clinton administration approved WTO membership for China in 2000. However, the US claims that China has failed to fulfill its promise to implement reforms and meet the requirements of WTO membership, and that flaws in the rules of the current trading system allow China to limit imports with high tariffs and discriminatory regulations, to subsidize exports with an inexpensive currency and readily available credit on easy terms (courtesy of state controlled banks), bully foreign investors, and pirate western intellectual property. The US claims that the WTO has declined to take action against China's "cheating".

China had agreed to purchase "a very substantial" amount of soy beans and other agricultural, energy, industrial, and other products from the US. China had agreed to reduce the 40% tariff on cars imported from the US, although Beijing had yet to confirm this as at December 4, 2018. The Chinese government was considering a reduction in the auto tariff but provided no specifics. China and the US had agreed to immediately begin negotiations on structural changes with respect to forced technology transfer, intellectual property protection, non-tariff barriers, cyber intrusions and cyber theft, services, and agriculture. The two countries agreed to halt the mutual increase of new tariffs and China undertook to increase its purchases from the US so as to "gradually ease the imbalance in two-way

trade". The official announcement from Beijing was silent about such purchases, but stated that both leaders were striving to reach a mutually beneficial agreement.

On October 17, 2018, the United States announced its withdrawal from the Universal Postal Union, in order to renegotiate international shipping rates for mail and small packages. China had been paying lower rates because it was considered a developing nation; the United States intends to charge the same rates for all countries.

### **3. 7 Influence of USA-China Trade War on International Business**

#### **3.7. 1 US Executive Branch**

The planned Chinese tariffs only amounted to 0.3% of US GDP. These moves would have "short-term pain" but "long-term success". It could be argued that tariffs are self-defeating and that renegotiating China's WTO membership [64] would be a more effective measure. The US economy remained strong in 2019. Interest rate increases were necessary to contain inflation. Given this outlook of strong growth, a strong labor market, and inflation close to the US goal, and taking account of all the various risks surrounding this outlook, further gradual increases are probably the best means of sustaining economic expansion.

A self-appointed group of billionaires with links to Goldman Sachs and Wall Street pressed on the White House, claiming that this was part of a Chinese government operation that was undermining the US negotiating position. They called for foreign agents to be deregistered if found to be interfering with negotiations or violating the Foreign Agents Registration Act, urged investment in factory towns, e.g. Dayton, Ohio, that need a rebirth of their manufacturing base.

#### **3.7.2 Strong Bipartisan Pushes to Broaden and Strengthen Sanctions Against China**

Democrats, Republicans, Americans of every political ideology, and every region in the country should support higher tariffs on China in retaliation for their country being taken advantage of. Most Democratic senators, including Committee ranking members Bob Menendez (Foreign Relations), Sherrrod Brown (Banking), and Ron Wyden (Finance), called for Americans to confront the rampant theft of US intellectual property, forced data storage localization policies, agricultural policies that disadvantage American farmers, the dumping shoddy of goods, restricted market access for US service providers and manufacturers, and

mercantilist industrial policies that have cost US workers their jobs. They called for sanctions on Chinese companies, such as ZTE, which has allegedly sold sensitive US technologies to Iran and North Korea and repeatedly made false statements. The Democrats have further called for putting American workers, farmers, businesses, innovation and national security ahead of China and have remained steadfast in enforcing US laws against predatory and abusive behaviors. The Senators have requested that the administration push harder for genuine structural reforms in China.

China is a greater threat to American manufacturing and high-tech industries, and is heavily involved in industrial espionage. China is thought to be responsible for 50-80% of cross-border intellectual property theft worldwide, and over 90% of cyber-enabled economic espionage in the US.

The US definitely needs to take strong, intelligently thought out, and strategically effective action against China's brazenly unfair trade practices. However, it needs to do a lot more to support US workers and products than simply confront China over its bad behavior. Beijing's regulatory barriers, localization requirements, labor abuses, anti-competitive policies, and many other unfair trade practices require a full and comprehensive response. The US has to show moral courage and be prepared to use its economic leverage to not only guarantee free trade for American products in Chinese markets, but also to advance human rights in China and Tibet.

A brief reduction in the trade deficit did nothing to solve the main challenges of the trade relationship. These are going to require "targeted sanctions" on Chinese companies, non-tariff restrictions, and upgraded protection for US intellectual property innovation. US public opinion remains in favor of revoking China's most favored nation status and for waging trade war against that country.

### 3.7.3 Markets and Industries

The tariffs had brought about positive and negative results as early as July 2018. A number of industries were evincing employment growth while others were planning layoffs. Stock prices in the US and China fell significantly four to six weeks prior to the tariffs going into effect. Trade war fears had led to a bear market in China. By late June, the country's stock market has lost 20% of the value it had the beginning of 2018 when it reached record levels. The Japanese Nikkei 225 also suffered a "three-

week pullback". When the tariffs went into effect (on July 6, 2018), the markets rebounded and rallied due to a positive jobs report in the US. Asian markets similarly rebounded, ending the day on a high note. According to the Associated Press, this positive response to the tariffs in the US and Asian markets was due to the end of uncertainty, and according to Investor's Business Daily, because the "markets had largely priced in the impact".

Announcements of US and Chinese tariff increases have prompted concerns from several major US industries. Organizations critical of the intensifying trade war included the National Pork Producers Council, the American Soybean Association, and the Retail Industry Leaders Association. Several mayors representing towns with a heavy reliance on manufacturing have also expressed their concerns. In September, a business coalition announced a lobbying campaign under the name of "Tariffs Hurt the Heartland" to protest the proposed tariffs. Proponents of the increased the US tariffs included Scott Paul, president of the Alliance for American Manufacturing.

### 3.7.4 Increase Protectionism Between the USA and China

The need to stay afloat on both global and national markets means that corporations will always look for ways to protect their profit margins. This obviously includes avoiding hefty tariffs. The costly price of building manufacturing infrastructure in the US has led corporations to turn their eyes toward countries eager to entice US manufacturing and jobs. Many companies are already looking to relocate their manufacturing facilities to China's neighbor, Vietnam. The global news magazine, *Foreign Policy*, reports that Goertek, a Chinese company that supplies Apple Air Pods, has already begun relocating its machines to Vietnam.

This is a decision that many companies will be forced to make. Coi Rubber President, David Chao, has stated that he had been considering offshoring manufacturing to countries in the proximity of China prior to the trade war talks. The passage of recent tariff laws only solidified Mr. Chao's decision to relocate the company's China factory to another competitive country in order to avoid unreasonable tariff costs and maintain the company's global expansion trajectory. Coi Rubber will continue to operate their three factories in China but will locate their primary factory in Vietnam. Although the tariffs may impact many manufacturers initially, Mr. Chao sees this as an opportunity to invest in Coi Rubber's future by

building their 4th factory in Vietnam, thereby allowing them to not only avoid high tariff costs but to reduce labor costs as well.

The decision of the US administration to impose a new round of tariff increases on imports from China has taken the US-China trade dispute to a new level. Import tariffs were increased 10 p.p., and steadily raised to 25 p.p. by the end of 2018. The new list considerably expanded the range of Chinese products included in the first two tranches of US import tariff hikes. These were implemented on July 6 and August 23, 2018. The policy triggered immediate retaliation. China raised tariffs by 25 p.p. on similar amounts of imports from the US on the same dates that the US tariffs came into force.

This sort of protectionist tit-for-tat can have consequences for the economies of the warring parties, as the experience of the Great Depression illustrates [8] [34] [43]. Moreover, it can also affect third countries, especially those with close economic ties to the US and China. This paper provides novel partial equilibrium estimates of the potential trade and investment impacts of the US-China trade dispute, focusing on East Asia [14]. Countries in this region are the most exposed to the dispute by virtue of their integration with Chinese-led supply chains and the similarity of their export baskets with that of China.

We estimate the expected import response to the tariff increase. To do so we combine HS-8 digit US import data for 2017 from the US Census Bureau of Statistics, HS-6 digit product-level price elasticity of US imports [18][32][37][42][31][35] and the published lists of Chinese products subject to the three tranches of US tariffs. We assume the price of import to increase proportionately with the tariff, which is then multiplied by the relevant elasticity and the import value to obtain the expected reduction in US import from China.

Our calculations suggest that the total US imports from China in the affected products amounted to \$234.8 billion in 2017, of which \$188.9 billion have been targeted in the last tranche of tariffs (Table 1). Based on the data we use, the tariffs would reduce US imports from

Table 1: Value of US imports from China targeted by the tariff measures.  
China by \$68.6 billion, equivalent to 13.6% of total US imports from China and 3% of global Chinese merchandise exports. This expected drop in Chinese exports would translate into a reduction in domestic value added by \$41.4 billion, a relatively modest 0.3% of Chinese GDP. This is an upper bound of the direct impact on Chinese exports, as it does not

consider the possible re-direction of these exports towards third markets.

The bulk of the affected imports is concentrated in electronic equipment and machinery and their components (Fig. 3). Electronic and optical equipment (including TV and sound

Fig. 3: Expected drop in US imports from China due to US tariffs hike, by HS-2 digit sector (\$ million). recording devices) and their components, machinery, boilers and mechanical appliances account for almost half of the expected drop in US imports from China. A significant amount of the import drop is also expected in consumer products, such as furniture, vehicles, leather articles and fish and crustaceans, which may have some direct impact on parts of the typical US household consumption basket.

The upside of the reduction in Chinese exports to the US is the potential diversion of US imports towards non-Chinese suppliers, particularly in East Asia, where export structures are similar to the Chinese ones. The present study identifies Chinese products (at the HS-8 digit level) that are subject to higher tariffs in the US, and which other East Asian countries exported to the US in 2017 in order to give a sense of these potential export opportunities. It seems probable that a country that is exporting a non-negligible amount of a certain product to a certain market would be more likely to replace an existing exporter in that product-market pair [38].

According to this metric, the replacement potential of Chinese exports in the US by East Asian countries – especially emerging economies – is quite significant. Vietnam, the Philippines, and Cambodia are the East Asian countries with the largest replacement potential relative to the size of their economy (Fig. 4). The estimated drop in Chinese exports to the US

Fig. 4: Potential replacement of Chinese exports to the US, by countries (% of GDP).

(at values of at least 10 mln USD) is equivalent to 10.9% of Vietnam's GDP. This falls to 4.4% when the associated domestic value added of these exports is considered. The greatest opportunities lie in those products for which the expected drop in Chinese exports to the US (and which Vietnam already exports there) are large, e.g. chairs, insulated ignition, shrimp and prawns, travel bags, seat parts, television cameras, wooden furniture, and handbags (Fig. 5).

Fig. 5: Main potential products where Vietnam could replace Chinese exports in the US.

Cambodia exports a much smaller set of products with these characteristics, e.g. plywood sheets, handbags, travel and sports bags, lighting sets for Christmas trees, dog and cat food, seat parts, and bicycles. Taiwan [51], Singapore, Malaysia, and Thailand also have non-negligible export replacement potential. The potential replacement is more limited for Indonesia. The drop of Chinese gross exports to the US in products that Indonesia also exports there is equivalent to 1.3% of GDP, with an associated domestic value added of 1.0% of GDP [38].

By raising the cost of serving the US market from China, the trade war could also divert investment to third countries [14]. This diversion is most likely to affect investment seeking to by-pass US import tariff hikes. The extent to which investment intended to serve the US market can relocate to other countries partly depends on each country's ability to produce the same set of affected products and partly on perceptions about the duration of the trade war. The present study measures this ability through the correlation index between the expected drop in US imports from China and US imports from each East Asian country in those HS 8-digit products subject to the tariffs [38]. The value of the index is highest for Taiwan, followed by Thailand, Malaysia, Vietnam, and the Philippines, and lowest for Indonesia and Myanmar (Fig. 6).

Fig. 6: Degree of similarities of export baskets to the US with China for affected products (index of correlation at HS-8 digit).

While this ranking tries to capture only one of the several criteria used for investment choices, it is suggestive of the variation in relative attractiveness across potential destinations for investments based on an export basket similar to that of China [38].

While China has progressively absorbed large chunks of the value chain in various sectors [19][29], it still relies on imports of foreign intermediates and final inputs for some of its production. East Asian countries are key suppliers of such intermediates and inputs to China [14]. Hence, the expected drop in Chinese exports to the US may have knock-on effects on these countries via backward linkages. The extent of this impact would depend on which parts of the value chain each country contributes to. This in turn determines the intermediates and raw materials that other countries provide to China in the production of the products affected by the tariff hike [38].

In order to gauge the importance of this channel, the estimated drop in Chinese exports at the HS-8 digit level is matched with the country-specific

shares of domestic value added in Chinese gross exports to the US in those products (available from OECD TiVA data). Taiwan and Malaysia are the East Asian countries [51] that appear most vulnerable to the drop in Chinese exports via the supply chain with an estimated GDP loss of 0.24% and 0.20% respectively [38] (Fig. 7).

Fig. 7: Estimated effects of US-China trade war on GDP via supply linkages.

This is mainly due to the fact that they provide inputs for Chinese exports to the US in electronic and optical equipment, as well as electrical machinery, which accounts for two third of this loss. Singapore, South Korea, and Thailand are all expected to lose more than 0.1% of their GDP via this channel, while the results for Cambodia, Indonesia and Vietnam are relatively muted due to the low participation in Chinese-led global value chains [14].

While these negative effects are smaller than the estimated (positive) export replacement potential, the two figures are not necessarily comparable. The latter are upper bound estimates of the potential for replacement. The true dimension of the replacement effect is likely to be considerably smaller for two reasons: first, each country would be competing for the same potential market; second, any such replacement would hinge on the supply response in each country-product pair, which could be relatively small (and even zero) in many cases. By contrast, the effects via the supply chain are likely to provide a more precise order of magnitude of the actual losses [38][36].

This type of analysis could help policymakers in East Asia (and beyond) identify the potential winners and losers among domestic producers from the US-China trade war [14]. Governments could help the former replace Chinese exports to the US through measures such as facilitating access to imported inputs, which are heavily used by East Asian exporters, and ensuring the availability of the finance, including trade finance, that will be required for the additional production and exports [38]; [36]. At the same time, assistance to potential losers to reallocate their production and/or their labor could help minimize the domestic costs of the trade war [6].

### **3.7.5 China in a Trade War with the USA and its other Trading Partners**

The US Administration deserves credit for taking a harder line towards Beijing, both at home and abroad. Attacking Chinese protectionism [29][30] now has bipartisan support in Washington and Berlin, and in 2018, the United Kingdom joined the

United States in imposing tighter restrictions on Chinese investment. But their critics claim that they have not done enough to capitalize on those shared grievances. If anything, they have achieved the reverse. For example, in 2018, they alienated European and Japanese officials by imposing tariffs on their steel and aluminum to the US.

China has tried to defuse the global irritation over its mercantilist stance by signaling a willingness to revise its “Made in China 2025” program of state subsidies and market share targets. This recent flexibility comes as Chinese industrial production figures at the end 2018 year fell short of economists’ expectations and retail sales were growing at their slowest rate in 15 years. Analysts in China and the United States say China is modifying the “Made in China” program because of pressure from all its major trading partners.

The US Trade Representative Robert E. Lighthizer has claimed that this subsidy program, which sets market share goals for Chinese industry, imperils US technological hegemony. China wants its semiconductor manufacturers to provide 70% of domestic needs, up from less than 20% today. At stake are 6 bln USD in annual US exports. But roughly a dozen other countries are even more dependent on high-tech manufacturing and exports of advanced factory gear, and are more exposed to China’s desire to replace purchases of foreign products with domestic alternatives, according to the Mercator Institute for China Studies in Berlin.

The pushback from other trading partners is a crucial factor in the dynamic development of China. That’s because the Made in China 2025 program is more of a threat to Germany, South Korea and Japan than it is to the United States. External pressure drove China to open markets for financial services and automobiles, according to economist Andrew Polk, a partner in Trivium China, a Beijing-based consultancy.

At the end of 2018, the EU agreed to establish a new foreign investment screening mechanism. This initiative was largely motivated by a sharp increase in Chinese activity on the continent [30][39]. However, it leaves final decisions to national governments. As such, it is less effective than the Committee on Foreign Investment in the United States. The German government blocked two potential acquisitions by Chinese investors in July 2018. This came on the heels of similar action by Canada two months earlier. Germany also lowered

the level of foreign ownership that requires government review from 25% to 15%.

With the United States and China locked in a geopolitical competition, it is easier for revision-minded officials to advocate changes in programs like Made in China 2025 by citing shared concerns among the country’s major trading partners. The Chinese authorities have changed course under pressure before. In 2015, they scrapped plans to require foreign financial institutions to install Chinese software after complaints from US, European and Japanese diplomats and business groups. Some administration officials scoff at the proposed changes as being cosmetic and designed to sap US negotiating resolve. Michael Wessel, a member of the US-China Economic and Security Review Commission, described the plans to allow foreign companies a greater role in the Chinese technology program were “an influence operation at its best”. He also questioned whether Chinese laws would mean much so long as the courts remained under the control of the Communist Party. “What the Chinese are talking about are really just baby steps”, he said [23].

On June 1, 2018, following similar action by the US, the EU initiated legal proceedings against China in the WTO, alleging that by compelling foreign firms to grant ownership and usage rights of their technology to Chinese entities, China was discriminating against foreign firms and undermining the intellectual property rights of EU companies [30][39]. EU firms were allegedly forced to establish joint ventures as a precondition for gaining access to the Chinese market. The European Commissioner for Trade, Cecilia Malmström, said “We cannot let any country force our companies to surrender this hard-earned knowledge at its border”. This is against international rules that we have all agreed upon in the WTO. American, European and Japanese officials have discussed joint strategy and taken actions against unfair competition by China [30]. The 2018 G20 Summit in Buenos Aires concluded the multilateral trading system “is currently falling short of its objectives ... necessary reform of the WTO to improve its functioning” [44] [30].

## 4 Conclusions

Foreign trade policy plays a key role in the maintenance of both economic and political liberalization. Rent seeking can have far-reaching implications for a country’s economic development. This is especially true in underdeveloped and transitional countries, where it can take scarce

resources from productive areas and use them to promote and/or perpetuate rents.

Structural and micro-political economy analyses of foreign trade policy in the context of sustainable development invariably fail to factor in the impact of the recent reappraisals of protectionism and the relatively fixed nature of the institutions designed to handle domestic producer complaints. The political consensus on foreign trade policy and protectionism has changed over time. Tariffs and other forms of protectionism assume greater prominence in the policies of political parties during a recession. However, even during a recession, there is usually a modicum of support for a liberal foreign trade policy in a market economy. No foreign trade policy is purely liberal or purely protectionist. Foreign trade policy tends towards liberalism during periods of rapid economic growth and protectionism during downturns.

A tariff trade war will inflict considerable harm on China in all indicators, including welfare, GDP, manufacturing employment, and trade. However, China should nevertheless be able to sustain the costs, and its economy should not be severely damaged. As for the United States, the simulation predicts it will gain on welfare, GDP and non-manufacturing production, but lose on employment and trade (both export and import). As these are by far the two largest economies on the planet, their actions inevitably affect the entire world. The simulation therefore predicts that the rest of the world will feel the impact of any trade war between them.

Most large and developed nations will benefit from a US-China trade war. As trade decreases between the United States and China, it will presumably increase between other nations. For example, Chinese and international rubber producers are preparing to restructure their supply chains by relocating their manufacturing facilities from China to Vietnam and Malaysia. However, smaller nations will see significant negative impacts. For example, the world's total welfare, GDP, manufacturing production and employment, export, import, and total trade are expected to decrease since many of these nations are highly trade dependent.

China is not merely romanticizing its historical legacies; there are painstaking economic and geopolitical calculations underpinning its strategies for the 21st century. It is important to pay heed to changing trends in the international trade regime. Commercial relations are too important to be held hostage to political grandstanding or airy rhetoric from politicians performing for domestic galleries. Disturbing these relations would have ramifications

for sales, growth, and employment – especially in this day and age of COVID-19 [36]. Commercial imperatives can pose political dilemmas for autocratic regimes such as China. Again, this applies a fortiori with respect to the COVID -19 pandemic [36].

The Global Financial Crisis of 2007–2008 (GFC) was a total shock to the comparison in cost savings. Global supply chains became more costly when the risk of a non-delivery of an input good increased substantially after the Global Crisis. Firms may have also expected higher tariff rates after the Global Crisis, which shrinks advantage of GVCs as input goods pass the border several times. At the same time, the Global Crisis made robot adoption less costly, with the sharp decline in interest rates relative to wages when central banks started to fight the adverse effect of the crisis. As a result, many firms in rich countries like USA started to re-shore production back to their home country and invested in robots instead.

In the wake of the Global Crisis, uncertainty in the world economy led many firms to reassess their business models. Rather than relying on global supply chains, an increasing number of firms invested in robots, which prompted a renaissance of manufacturing in industrialized countries like USA. Changes in the world economy due to COVID-19 make a V-shaped recovery from the coming recession unlikely, more likely is U and in services L. Instead, COVID-19 will accelerate the process begun after the Global Crisis by encouraging firms to re-shore activity back to rich countries like USA [36].

A great deal has depended on the attitude of the US and its allies during the conflict between Russia and Ukraine. Unless they agree to a compromise, paid for by Ukraine, this will be a long-drawn-out guerrilla war. The conflict with the West, which has already moved into the military phase in Ukraine, and which will continue to be played out in parallel in the political, diplomatic, media, economic and virtual worlds (hacking attacks have been ongoing for a long time and show no sign of letting up), could eventually exhaust Russia's forces and deplete its resources. If this scenario came to pass, Russia might well be plunged into an economic crisis comparable that which afflicted the USSR during its final days.

In this context, the world economy has entered a phase of geopolitical turbulence that will have enormous economic and financial consequences far beyond Ukraine. A hot war between the major powers sometime in the next ten years is on the cards. Price shocks will have a negative impact

worldwide, especially on poorer households, as food and fuel account for a higher percentage of their expenditure. If the conflict escalates, the damage to the world economy will be even more devastating. The sanctions imposed on Russia will have a significant impact on the global economy and financial markets, and significantly poison other countries. The monetary authorities will need to carefully monitor the spillover of rising international prices onto local inflation in order to prepare the right responses. State fiscal policies will have to support the most vulnerable households to counterbalance the rising cost of living.

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The author equally contributed in the present research, at all stages from the formulation of the problem to the final findings and solution.

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#### **Conflict of Interest**

The author have no conflicts of interest to declare that are relevant to the content of this article.

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### Figures and Table

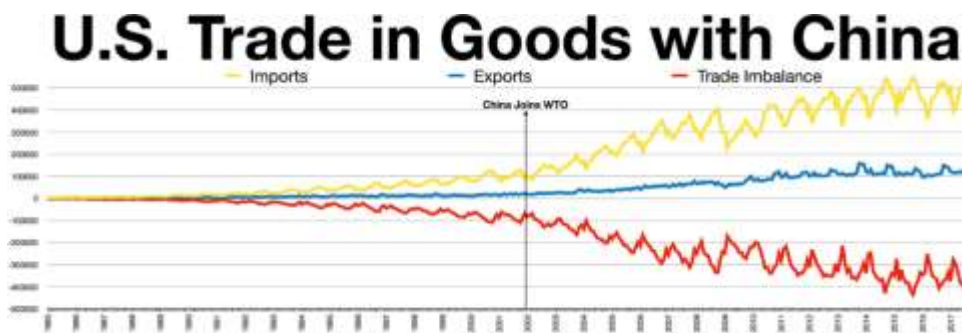
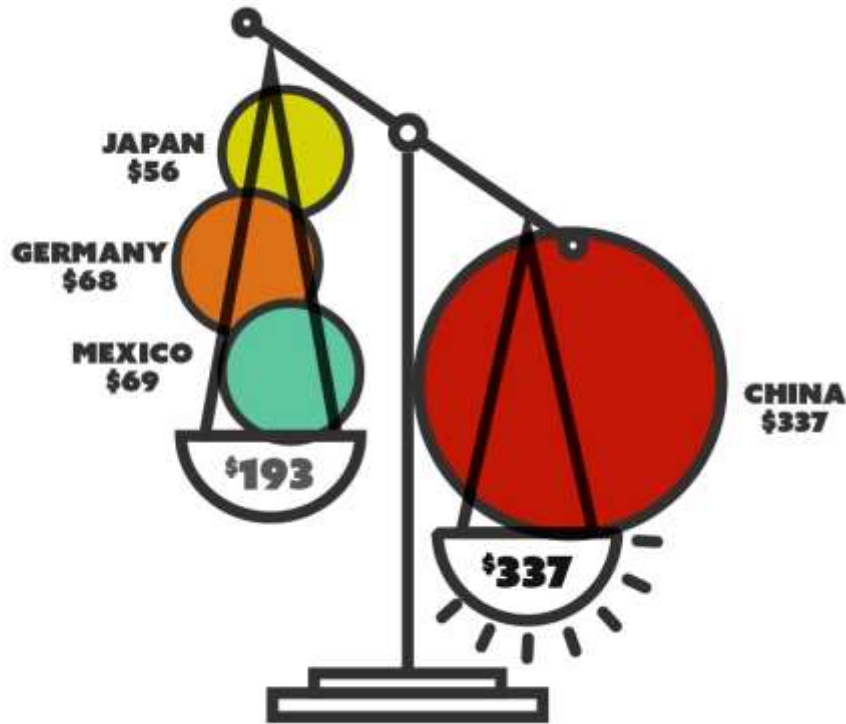


Fig. 1: The rapidly increasing US trade imbalance with China.

## U.S. TRADE DEFICIT BY COUNTRY IN BILLIONS OF DOLLARS



SOURCE: OFFICE OF THE U.S. TRADE REPRESENTATIVE

Fig. 2: US Trade Representative.

Table 1: Value of US imports from China targeted by the tariff measures.

	Value of target imports in first announcement (in \$ bn)	Value of target imports at effective date (in \$ bn)
1 <sup>st</sup> tranche	32.3 (April 3 <sup>rd</sup> )	32.3 (July 6 <sup>th</sup> )
2 <sup>nd</sup> tranche	13.8 (April 3 <sup>rd</sup> )	13.7 (August 23 <sup>rd</sup> )
3 <sup>rd</sup> tranche	197.2 (July 10 <sup>th</sup> )	188.9 (Sept. 24 <sup>th</sup> )
<b>Total</b>		<b>234.8</b>

Source: M. Cali, The impact of the US-China trade war on East Asia, 16 October 2018, <https://voxeu.org/article/impact-us-china-trade-war-east-asia>, 4.01.2019.

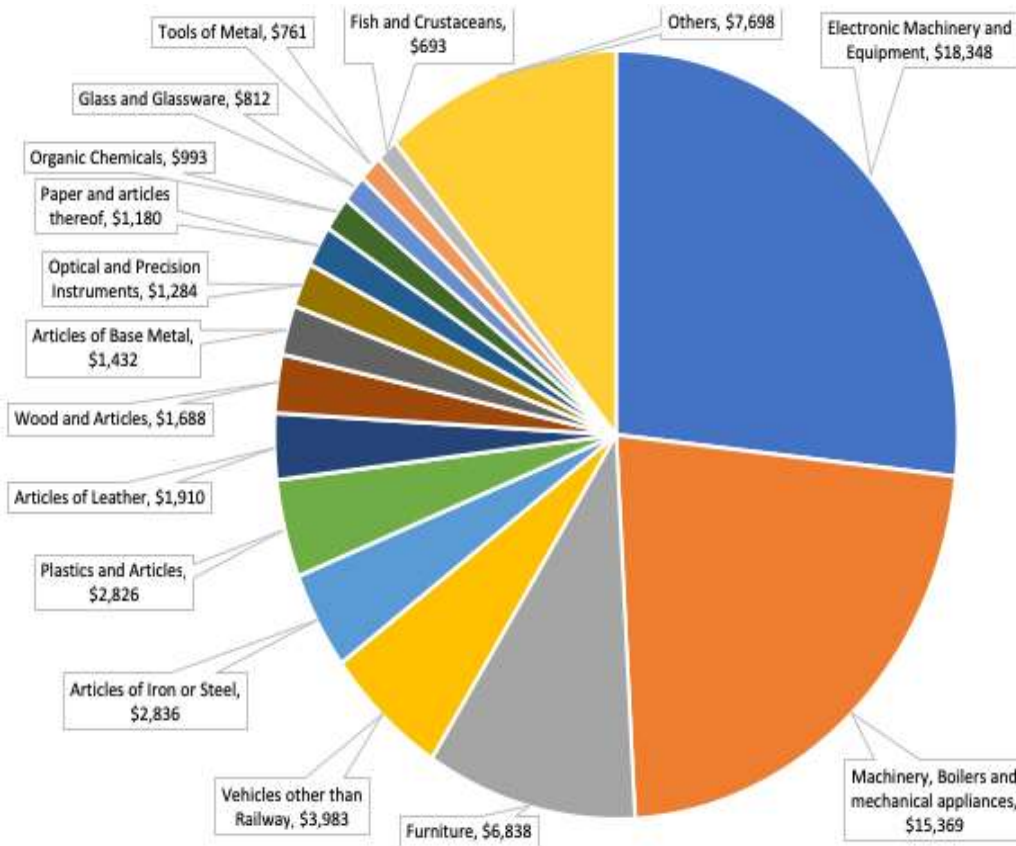


Fig. 3: Expected drop in US imports from China due to US tariffs hike, by HS-2 digit sector (\$ million).

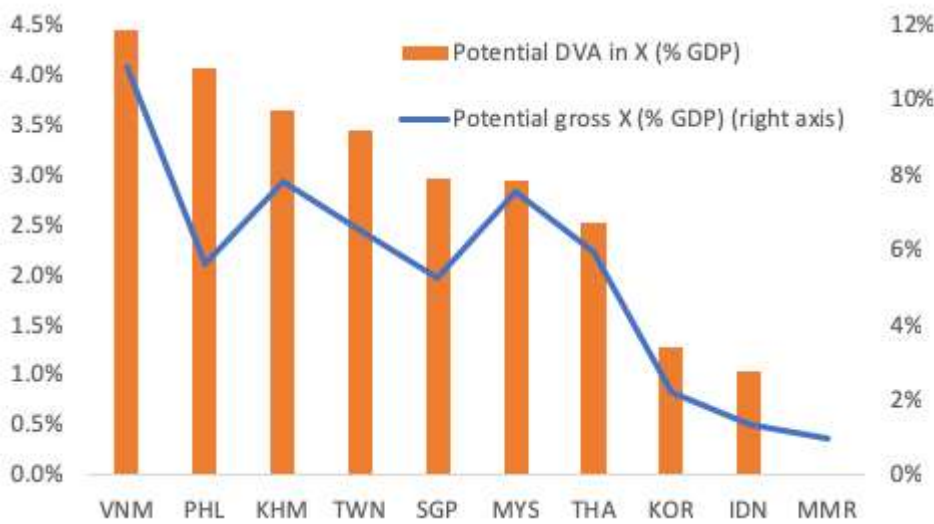


Fig. 4: Potential replacement of Chinese exports to the US, by countries (% of GDP).

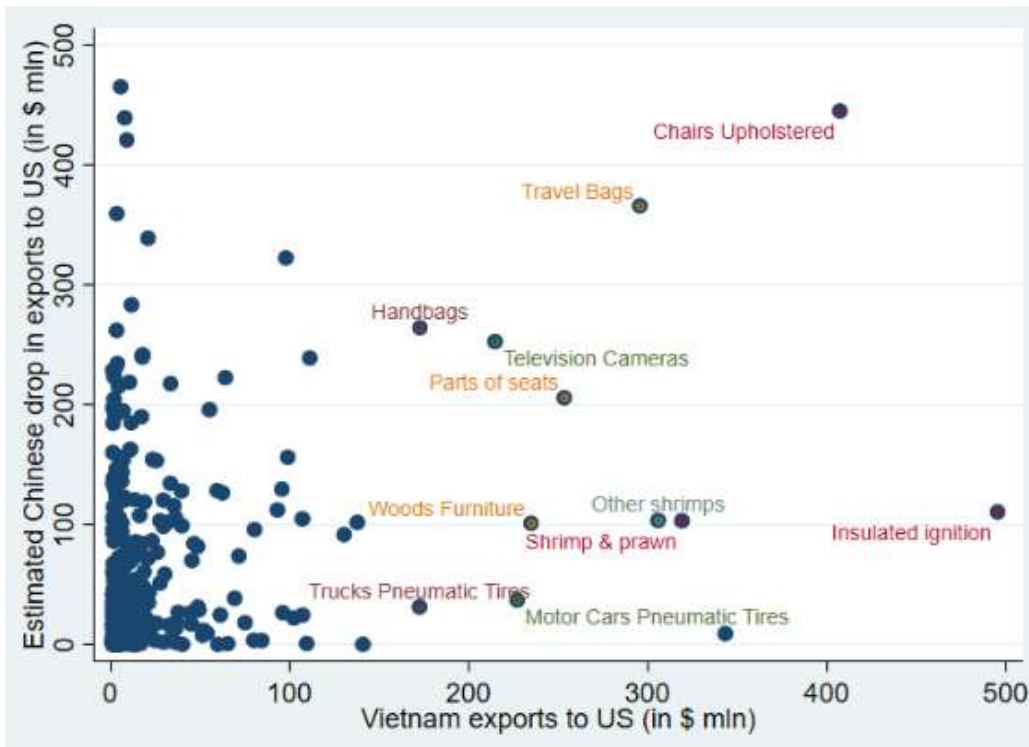


Fig. 5: Main potential products where Vietnam could replace Chinese exports in the US.

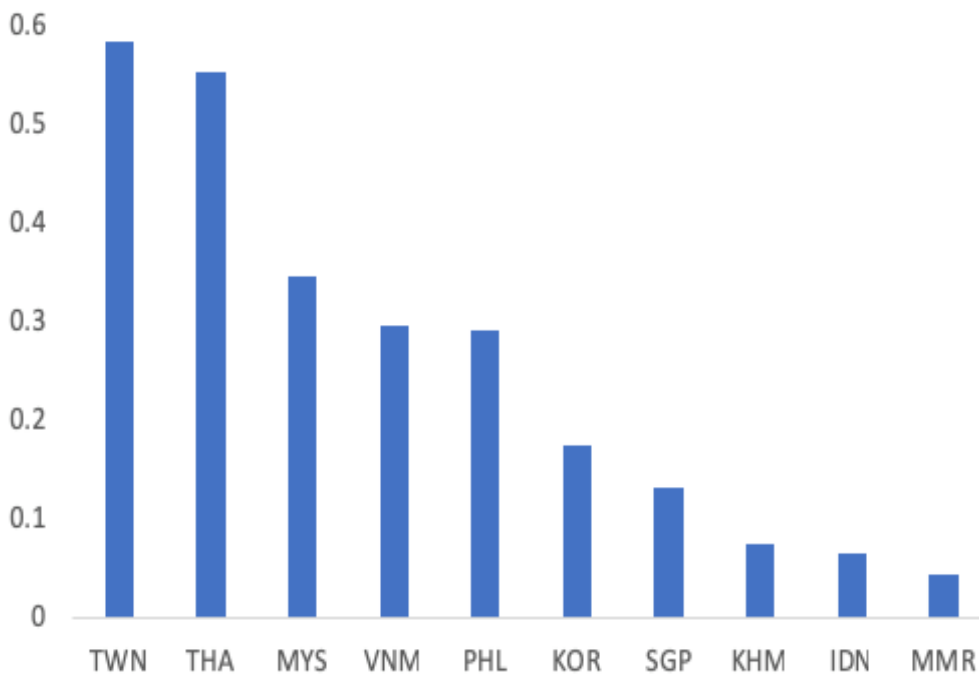


Fig. 6: Degree of similarities of export baskets to the US with China for affected products (*index of correlation at HS-8 digit*).

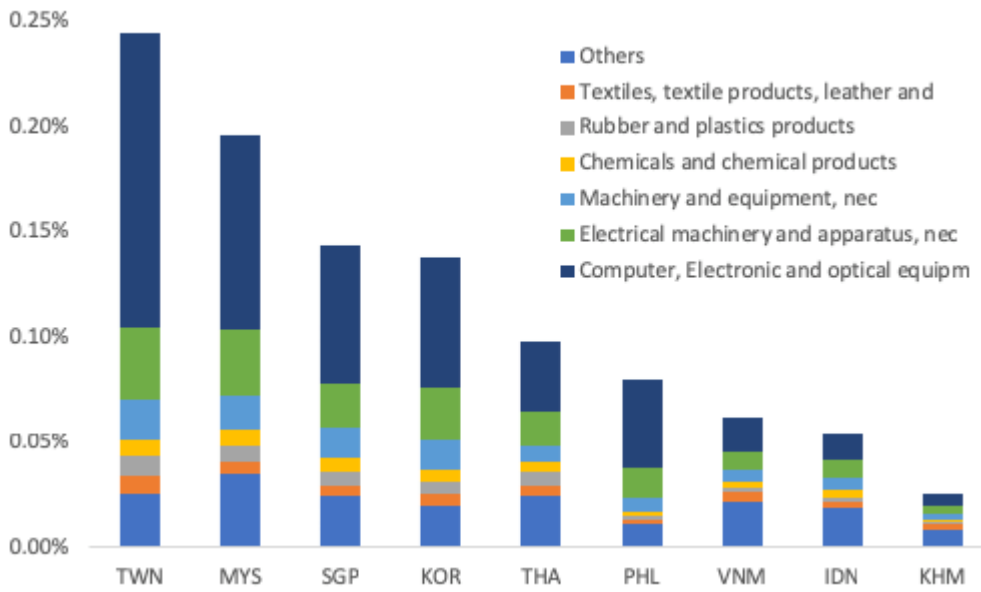


Fig. 7: Estimated effects of US-China trade war on GDP via supply linkages.