US–China Trade amid COVID-19

Image source: Reuters

Devassy Auseph

It is a fact that the US has the greatest trade deficit with China, with over 22 per cent[1] of annual US imports from China. In 2019, the US imported Chinese goods worth around US$ 452.2 billion, a significant portion of which are consumer goods, whose parent companies are headquartered in the states that have outsourced their production to emerging countries, mainly China. The ongoing trade war has resulted in sharp decline in bilateral trade, higher price for end consumers and trade diversion effects for countries not directly involved in the trade war. The fact that even after levying substantial tariffs, Chinese goods maintain 75 per cent of their exports to the US reflects first, how competitively priced are Chinese goods and second, the price elasticity for consumer goods by the American working class. However, US President Donald Trump, from the time of his presidential campaign, has been a strong advocate of trade protectionism, 'Americanisation' and domestication. In one such instance, he had been quoted "I want to stop unfair transfer of American technology and intellectual property to China" in line with his political rhetoric of Make America Great Again.

Trade War's Effect on the World Economy

What did it entail for the world economy? Two manufacturing powerhouses, which account for a combined 38 per cent[2] of global manufacturing, engaged in escalating trade tensions. The US and China were embroiled in a tit for tat trade war starting from 2018. Initially, Washington imposed two rounds of tariff on US$ 250 billion worth of goods at 25 per cent, which was retaliated in kind by Beijing; subsequently a third round of tariff was imposed by Washington on goods worth US$ 200 billion at 10 per cent that was to be later increased to 25 per cent. However, China was held in a state of political limbo, fearing further repercussions and economic volatility, which resulted in economic adviser to president of China, Liu He and General Secretary Xi Jinping paying Washington a visit.

Analysis shows that the US tariffs caused a US$ 35 billion blow to Chinese exports, causing approximately a 25 per cent net export loss. However, consequently there has been a corresponding trade diversion effect. About 63 per cent of export losses were diverted to other countries and remaining 37 per cent were captured by domestic producers. Office machinery and communication equipment sector were hit the hardest suffering a loss of US$ 15 billion, with Taiwan gaining an additional US$ 4.2 billion in additional exports. Second largest net gainer was Mexico, which increased its export to the US by US$ 3.5 billion mostly in the agri-food, transport equipment and electrical machinery sectors. The European Union also saw a significant increase in value of exports, around US$ 2.7 billion in the machinery sector.

Bilateral Trade, Trade Deficit and COVID-19

Coming to bilateral trade, the majority of imports to China are capital intensive manufacturing goods, planes, helicopters and spacecraft at 10 per cent; cars at 8.7 per cent and integrated circuits at 5.8 per cent. However, a significant portion of the goods are primary goods, of which 11.04 per cent are agricultural goods with soybeans at 9.3 per cent. Other major products are petroleum, petroleum gas and other mineral products standing upwards of 5 per cent[3] and precious metals like gold at 2.0 per cent. Similarly, China— the factory of the world— exports a fifth of the total export volume from China to the US. The major products exported from China to the states are sophisticated, capital intensive goods. The majority of it falls under the sub category of machines which comes more than 32.5 per cent[4]; these include broadcasting equipment at 14 per cent[5], computers at 9.8 per cent and office machine parts at 5.7 per cent.

The US invariably holds its biggest trade deficit with China. The US exports to China stood at US$ 110.5 billion in 2012, peaked in 2017 at US$ 129.9 billion and fell to US$ 106.6 billion in 2019. Correspondingly, the US imports from China stood at US$ 425.6 billion, climbed steadily and fell to US$ 452.2 billion in 2019. However, in spite of the tariffs imposed, the US imports from China was the highest for the year 2018 at US$ 539.5 billion. This is reflected in the US–China trade balances, which showed the largest negative balance for the year 2018 at US$ -419.2 billion.

In late 2019, with Wuhan becoming the epicentre of the coronavirus outbreak, the existing narrative took a turn. COVID-19 became an imminent looming threat not only for the two nations but the whole world. The outbreak was declared a public health emergency of international concern on January 30, 2020. Globally, with 1.2 million infected and 70,000 deaths, medical cooperation is a necessity. The two countries should immediately start working together for developing a treatment protocol or even better a vaccine. The US Centres for Disease Control and Prevention's technical assistance programme on infectious diseases in China should be restored.

However, both the nations have politicised COVID-19. Trump ally Tom Cotton has repeatedly alleged that the virus has been biologically engineered in a biochemical laboratory in Wuhan. On the flip side, Chinese foreign ministry spokesman Zhao Lijan suggests the US army personnel brought the disease to mainland China. Both the claims have been debunked. China's veteran ambassador to the US distanced himself from the conspiracy theories and acknowledged the fact, on record, that the US-China relationship needs de-escalation not denunciation.

Effects of COVID 19 on Global Economy and the Way Forward for US

It is an alarming fact that estimates by the International Labour Organization suggest that globally 2.7 billion employment would be affected by the new novel coronavirus, that is to say four in every five workers across the globe, and predict 25 million jobs are threatened. The worst affected sectors across the globe are food and accommodation (144 million), retail and wholesale (482 million), business services and administration (157 million) and manufacturing (463 million). It is necessary to understand that these sectors make up 45 per cent of contribution to the US economy of which manufacturing is the largest contributor at 18 per cent, followed by business services at 12 per cent. In the US alone, 6.65[6] million people filed claims for unemployment since COVID-19 was declared a pandemic.

The Dow Jones index, after the declaration of the pandemic, saw a 35 per cent decline which recovered back to -24.1 per cent. It recorded the worst one day fall since 1987. Central banks across the globe have eased monetary restrictions hoping investment will pick up. However, analysts are of the opinion that monetary measures alone would not suffice and fiscal measures are to be introduced. In the worst-case scenario, they suggest that the markets would be volatile till the pandemic is contained.

In China, industrial production fell by 13.5 per cent in the first two months of the year corresponding to 2019 for the same period. Chinese car sales have dropped by 86 per cent in February. Value of exports fell by 15.9 per cent and investment in fixed assets took the biggest blow by a fall of 24.5 per cent. By the end of February, Chinese unemployment rose to 6.2 per cent.

The majority of world economies have put themselves into a state of induced coma and for both China and the US coronavirus is a common enemy. What differently can the US do about it? It is necessary to understand that China holds a comparative advantage over the US mainly in two regards. First, a lower cost of living ensures that labour supply is abundant and surplus in China. Second, an exchange rate that is partially pegged to the US dollar. China's Yuan is fixed to a basket of currencies, including the US dollar. The partial pegging of Yuan ensures that the Chinese exports are competitively priced in the overseas market in spite of the overseas market volatility. Third, China is only second to Japan, in the volume of the US treasuries it has purchased and ultimately has become a lender nation to the US. As of November 2019, the US public debt to China was US$ 1.09 trillion. That is 16 per cent of the total public debt of the US owned by foreign countries. Experts are of the opinion that this gives China political leverage over the US fiscal policy and worry about what would happen if China started selling its Treasury holdings. It also would be disastrous if China merely cut back on its Treasury purchases.

What is the way forward? The US can employ COVID-19 to change the existing narrative. With coronavirus as the common enemy, both China and the US can cooperate to put an end to this trade war.

***Devassy Auseph is Research Intern at CPPR- Centre for Strategic Studies. Views expressed are personal and need not reflect or represent the views of Centre for Public Policy Research*.**

---

[1] https://www.census.gov/foreign-trade/Press-Release/current_press_release/exh1.pdf.
[2] https://www.brookings.edu/research/global-manufacturing-scorecard-how-the-us-compares-to-18-other-nations/.
[3] https://oec.world/en/visualize/tree_map/hs92/import/chn/usa/show/2017/.
[4] https://oec.world/en/visualize/tree_map/hs92/export/chn/show/all/2017/.
[5] https://oec.world/en/visualize/tree_map/hs92/export/chn/usa/show/2017/.
[6] https://www.bbc.com/news/business-51706225.