Trade war between the US and China: Who gains? Who loses? Does Malaysia stand a chance to benefit?

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Background

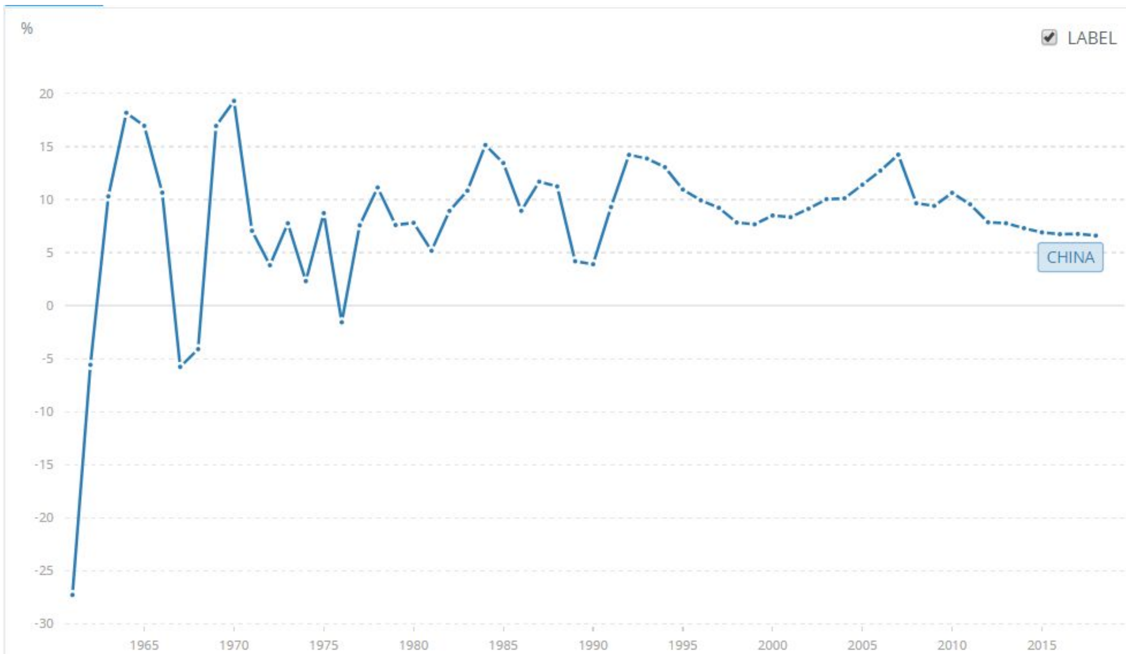

Fig 1.1 GDP growth rate for China
Source: World Bank

Since the 1980s, China has experienced huge and explosive growth in GDP with its GDP growth rate reaching as high as 19.3% in 1970 as shown in Fig 1.1 above. This was done based on a mixed economy system that involves both the private and public sectors and the massive government spending done by the Chinese government. This huge increase in growth is what led China to become the world's second-largest economy today with current estimates of its GDP at 13.6 trillion USD, estimates even suggest that China is bound to overtake the US as top dog economy in the world. This has led to a growing battle for economic and technological dominance between the world's two biggest economies.

Ever since Trump became president, he started to make comments on how China is "stealing" hundreds of billions of dollars from the US economy. As Trump asserted that it is shown through the trade deficit with China, multiple economists have debunked and accused Trump of mischaracterizing what a trade deficit is. This trade deficit is the balance of trade where it is the difference between the value of a country's imports and exports given a time period, a deficit means that the country has imported more goods than it has exported while a surplus is the opposite. Given most of China industries are still in the manufacturing sector, along with their artificially fixed exchange rate, this makes the Chinese exports more competitive than others. Shown below are the data that Trump was referring to when he is talking about a trade deficit.

2018 : U.S. trade in goods with China

NOTE: All figures are in millions of U.S. dollars on a nominal basis, not seasonally adjusted unless otherwise specified. Details may not equal totals due to rounding. Table reflects only those months for which there was trade.

Month	Exports	Imports	Balance
January 2018	9,902.6	45,765.6	-35,863.1
February 2018	9,759.9	39,020.6	-29,260.7
March 2018	12,652.1	38,327.6	-25,675.5
April 2018	10,503.8	38,303.9	-27,800.1
May 2018	10,428.2	43,965.7	-33,537.5
June 2018	10,860.1	44,612.1	-33,752.0
July 2018	10,134.6	47,120.6	-36,986.0
August 2018	9,285.9	47,869.2	-38,583.3
September 2018	9,730.0	50,015.0	-40,285.0
October 2018	9,139.9	52,202.3	-43,062.5
November 2018	8,606.2	46,500.8	-37,894.6
December 2018	9,144.9	45,972.1	-36,827.2
TOTAL 2018	**120,148.1**	**539,675.6**	**-419,527.4**

Fig 1.2a Trade of Balance between the US and China in 20180
Source: United States Census Bureau, Foreign Trade

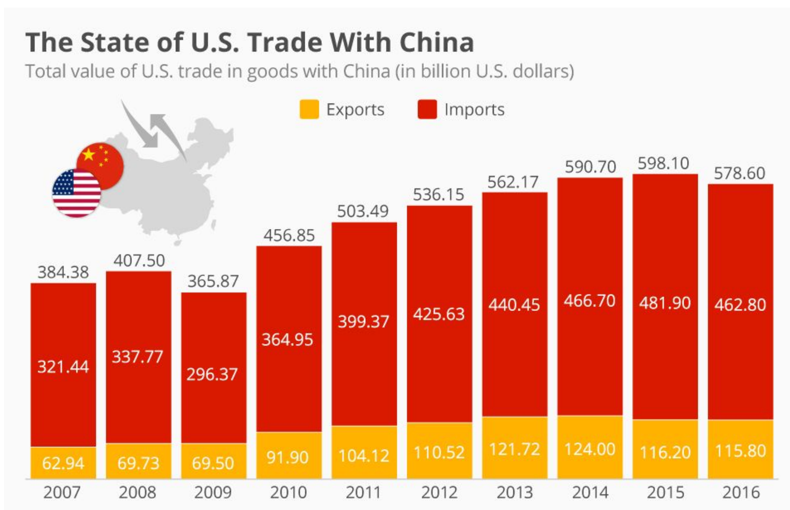

Fig 1.2b Trade of Balance between the US and China from 2007 to 2016
Source: U.S Census Bureau, Dyfed Loesche

Although there is no fixed definition, a trade war is generally defined as a situation in which countries will try to damage each other's trade through extreme protectionisms such as the imposition of tariffs or quota restrictions. On the 22nd of January of 2018, Trump announced the first tariffs on solar panels at 30% and washing machines at 20% from China's exports. However the tariffs of solar panels and washing machines were not the first, the US soon imposed further tariffs on steel at 25% and aluminum at 10% during March. Soon after, multiple tariffs were imposed by the US on different goods and China finally responded by imposing tariffs on the 2nd of April 2018, finally kick-starting a trade war that lasted till present. Shown below in Fig 1.3 is a timeline of the tariffs imposed in 2018.

Fig 1.3 Timeline of the trade war for 2018
Source: Financial Times

Effects of the trade war on both the US and China.

In terms of macroeconomic impacts, there are no clear winners between the US and China as both of their real exports and GDP has experienced a decrease in growth rate. The immediate impact that the trade war has would be the volatility of the stock market. Investors fled stocks and other assets that are perceived as risky as the trade war continues. The Dow Jones Industrial Average, a key stock market index that indicates the value of the 30 largest companies in the US, has plunged 800 points or 3% on its worst day in 2019 so far.

The foreign direct investment (FDI) for both countries has also decreased from 2017 to 2018. The US had an FDI of US$24.39 billion in 2017, which decreased to -USD$317.72, Similarly, the FDI for China decreased from -USD$27.79 billion in 2017 to -USD$107.02 (World Bank, 2018a). This could be explained in the loss of investor's confidence as a result of the trade war which sparks volatility in the economies of the two countries, promoting risks. This meant a loss of FDI inflow which reduces the FDI of the two countries. The US seems to be the one with the heaviest loss as the US is where many foreign investors set their eyes on to invest, so naturally, they will be more prone to impacts of the trade war.

However on import and export terms, by looking at the numbers it seems that China is losing against the US. As of September 2018, tariffs were worth USD$60 billion for

China, while the US had a tariff worth USD$200 billion (Financial Times, 2018). This means as a result of the tariffs, the US gained a possibly greater government revenue than China.

By analyzing the current account balance for the US and China, it could be said that China had the most impact when comparing the current account balances from 2017 to 2018. In 2017, China had a current account balance of USD$195.12 billion surplus, however that decreased greatly during 2018 which is the year which trade war starts, it decreased to USD$49.09 billion surplus. While the US also had a similar impact, the country did not experience a large reduction in balance like China. The current account balance for the US in 2017 is a deficit of USD$449.14 billion, the deficit later worsened in 2018 to USD$488.48 (World Bank, 2018b).

Aside from economics impacts, there are social and political impacts as well. China has been growing exponentially over the past few decades and is slowly catching up to the US in all aspects. There is fear among the US that a communist country may overtake them and become the new global superpower. There may be political gains for the current US president as he can use this trade war as an advantage for the upcoming 2020 US Presidential Elections.

After taking everything into consideration, we conclude that there is no “winners” in this trade war. The real question is: Who will lose more in this trade war? Based on the economic data so far, the US seems to have much more to lose compared to China.

How does the trade war affect Malaysia?

China has always been Malaysia’s top trading partner since 2016, with total trade worth RM313.8 billion in 2018, whereas the US ranked 3rd below Singapore which China has approximately two times more trade than US statistically (Ministry of Finance, 2019a). As the US impose higher tariffs on China, trade between the two countries will reduce as well as the prices of goods and services or raw materials are more expensive. According to the Ministry of Finance, Malaysia’s exports are estimated to decline at approximately 0.08% as almost half of Malaysia’s exports are used in the manufacturing process of China’s products, which these products are exported to the US. Due to lower export for Malaysia, it would also impact the GDP as it is estimated to reduce by 0.02% 2018 to 2020 (Ministry of Finance, 2019b).

If we dive deeper into the issue, a lower export will influence Malaysia’s labour force or investment. The unemployment rate in 2019 first quarter is 3.3% (Ministry of Finance, 2019a), which there is a possibility that the unemployment rate may increase due to labours made redundant as a result of cutting production.

Country	2018		2019 (Jan - Mar)	
	Number	Foreign Investment (RM million)	Number	Foreign Investment (RM million)
USA	18	3,155	15	11,494
China	40	19,673	22	4,406
Singapore	82	1,834	24	227
Japan	63	4,133	5	552
British Virgin Islands	5	2,769	1	548
Netherlands	10	8,337	4	355
Korea, Rep.	10	2,495	5	245

Fig 2.1 Foreign investment in Approved Manufacturing Projects
Source: Fiscal and Economic Division, Ministry of Finance Malaysia

By analysing this data table, the US seems to have invested greatly in Malaysia, approximately 4 times more than last year in 2018, and this is only at the first quarter of 2019, which more investments are expected to flow into Malaysia for the next three quarters. As for China, it seems that investment has slightly decreased at RM4406 million, which is lower than 2018's quarterly average of RM 4918.25 million though it may increase in later 3 quarters. However, the biggest take away from this is that the US heavily invested in Malaysia, and this may offset the decline in exports, GDP and unemployment rate in the long term in the manufacturing sector of Malaysia, the largest industrial sector in Malaysia as opportunities to expand production rises for businesses.

As the China's central bank, "The People's Bank of China" attempt to depreciate Chinese Yuan, it also affected the exchange rate of the Ringgit Malaysia (RM) and Chinese Yuan as the Chinese Yuan depreciates against the RM, specifically from 17 April 2019 to 28 August 2019, from 1 Chinese Yuan= RM0.62 to 1 Chinese Yuan= RM0.59. As the value of Chinese Yuan depreciates, exports from China will become cheaper which is the intention of China's central bank, to offset the burden caused by the trade war as tariffs from the US and China rise against the two countries. As an effect, this would encourage Malaysia's import from China to increase. In the first quarter of 2019, Malaysia's import from China is RM71.2billion, which is exceedingly higher than 2019's quarterly average of RM43.73billion, this signifies Malaysia's increasing demand and expenditure on China's imports (Ministry of Finance, 2019a).

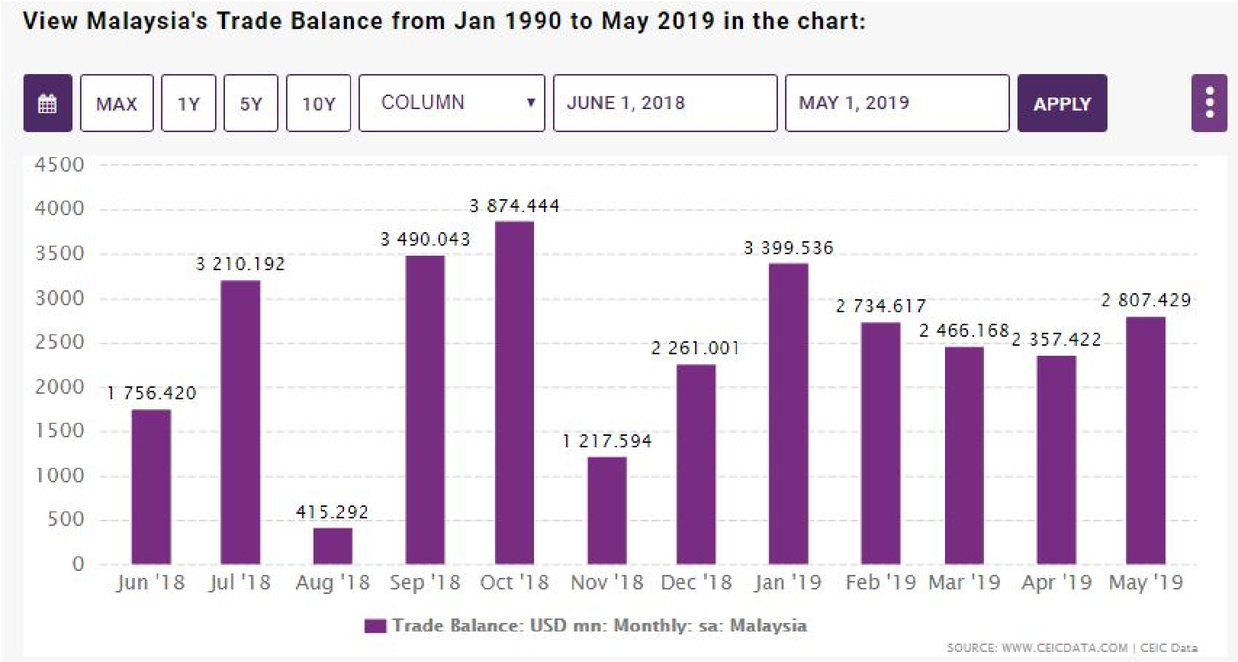

Figure 2.2 Malaysia’s Trade Balance
Source: CEIC Data

Cumulatively as a result of declining exports and increasing imports, this will have an impact on Malaysia’s balance of trade which it worsens. Evidently, in the first quarter of 2019 at January to March, Malaysia’s trade balance from January declined from $3399.54 million USD to $2466.17 million USD in March. Conclusively, it does not seem Malaysia has benefitted from this trade war between the US and China as it affected Malaysia’s trade balance to decline which isn’t a good change for Malaysia, as this also impact and worsens Malaysia’s current account balance as well. However, it is safe to say that Malaysia is not at a dangerous position, as Malaysia is able to overcome the impact of trade war through Free Trade Agreements, such as the ASEAN regional Free Trade Agreement and the bilateral Free Trade Agreements with Japan. Mayhaps, this is a blessing in disguise, as a result of this trade war, Malaysia is encouraged to diversify their trade with more countries rather be majorly dependent on their major trading partners, the US and China. This would allow Malaysia to spread the risk, should the trade war intensifies in the future.

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Figure 2.1. Table on Foreign investment in Approved Manufacturing Projects. Reprinted from 'Ministry of Finance'. Retrieved from https://www.treasury.gov.my/pdf/ekonomi/Indicators-062019/Indc-June-2019.pdf?fbclid=IwAR1IGm-KmG53NFALBKxU4jhddW674azwtfjEAn7mUfrqY7SQ8nXzLVvKqUU

Figure 2.2. Bar Chart on Malaysia's Trade Balance. Reprinted from 'CEIC'. Retrieved from https://www.ceicdata.com/en/indicator/malaysia/trade-balance

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