

The Spillover Impact of the US-China Trade War on India's Economy

Shaotian Chen*

Shenzhen college international education, Shenzhen, China

*Corresponding author: s21150.chen@stu.scie.com.cn

Abstract. This paper discusses the impact of the US-China trade war on India. Since it had been a fierce event in the past few years, the trade war had become a popular topic. The economists and politicians had predicted and discussed how the war will develop between the two superpowers, however, the impact on specific countries still needs to be further discussed and clarified. To discuss further of this topic, first, the background was further understood from the research. Then by discussing both positive and negative effects with data and details, finally analyzing whether there are benefits for India or not from the trade war between the two superpowers. During writing this template we found out that whether the US-China trade war will have a positive or negative impact on India depends on whether India had chosen wise politics towards the change in the global. India seems to be a great substitute for China, but it still has a lot of restrictions on the way of development.

Keywords: Demand & Supply, Foreign Direct Investment (FDI), Cost, Culture.

1. Introduction

This paper is going to discuss the impact of the US-China trade war on India. More details about the background will be discussed, then move on to the advantages and disadvantages of India.

The US-China trade war is an ongoing economic conflict between China and the United States. Initiated and launched by Donald Trump in January 2018, the specific content is that the United States sets tariffs and other trade barriers on China. China's economy has been growing rapidly in the past decade and is the fastest-growing economy among developing countries. However, due to China's economic growth, China often faces opposition from the United States over several issues, and the trade friction between China and the United States is increasing. The trade conflict between the world's two largest economies has influenced not only China and the US but the rest of the world. As the third largest economy in Asia and an important member of the WTO, India has been deeply affected by the trade war between China and the United States.

The content of the US-China trade war is: On April 4, 2018, the Office of the United States Trade Representative (USTR) published a list of suggestions on tariffs imposed on China. The list will impose a punitive tariff of 25% on 1,333 items (estimated at 50 billion USD) exported from China to the United States.

2. More Details about the US-China Trade War

Next, move on to a clearer analysis of the situation, exploring more about how those two superpowers make turmoil in the global market. As had been expressed in the introduction, the competition and conflict between China and the United States have been rapidly increasing nowadays. The impact of a trade war between the superpowers may have implications that may impact the global, also might bring a negative impact on other economies. However, this trade war might help India to tap the international market much easier than before if they can seize the opportunities well. According to data researched, in the first half of 2018, both US and China promoted about USD 50 billion in tariffs on imports from each other [1]. Later in September of the same year, this situation was accelerated in a worse way when the US imposed a 10% more tariff to cover Chinese imports worth 200 billion USD, and China struck back by introducing an additional USD 60 billion in tariffs on imports from the US [2].

One year later, in December 2019, the Situation became under control when both US and China agreed to stop introducing any new trade policies on each other and developed a reciprocal agreement to halt the trade war. However, this hadn't remained for long. Things did not happen successfully and stably just before the final talks were about to start between the two superpowers. Authorities from China rejected to change anything in their company-subsidizing laws and persist that the American government lifts the current tariffs on Chinese imports. Becoming furious at such a proposal from the Chinese authorities, the American President eventually doubled the rate of tariffs on China's imports from 10% to 20% on \$200 billion worth of imports from China. In vengeance, China halted all American imports of farm products [2]. In that case, unfortunately, the fierce war between the two of the most powerful economies continued.

The central bank in China had also decreased the currency of CNY above the reference rate of 7 CNY per USD, therefore, giving a hint about a raging war of currency between the US and China [2]. However, afterward, both China and US found out that the results of this currency war would turn out to be damage and destruction for both nations. To reduce the loss and destruction that can be caused by the currency war, in January 2020, both America and China agreed to halt the war. However, misfortune never comes singly. At the end of 2019, a global pandemic had exploded – Covid-19 is again menacing the relationship and the situation of international trade between the two countries [2].

3. More Details about the US-China Trade War

Even though the trade war between major economies in the world would cause harm to the global healthy economic environment. There are also some chances and opportunities generated in this game, and the ones who seize them may gain a lot from it, covering the costs of the trade war.

3.1 Demand and Supply Lead to Increase in Competitiveness

Referring to those data and background which had been previously discussed, one of the things we can tell is that the price of goods made in China will rise in the market of US, which infers, or also can be seen from the basic principle of economics: demand and supply. Demand means the number of goods that consumers have the willingness and ability to buy, and supply means the number of goods producers have the willingness and ability to sell. In most cases, price rises lead to quantity demand. Therefore, the competitiveness of goods from China decreases, and the US households turn to consume other substitutes.

As mentioned previously, in case China's export goods' competitiveness declines in the US market due to a rise in tariffs, this is allowing other countries, such as India, to replace "Made in China" with "Made in India" in the US, capturing more portion of US market. Since the exports from China to the US is several times the exports of the US to China before the trade war (2007-2017), after the restrictions set by the US in the trade war towards China's goods were announced, there will be a shortfall caused by the unsatisfied demand [Fig.1].

If India can realize and use this wonderful opportunity with caution and wisdom, making the right choice on policy, this will lead to a rise in aggregate demand in India, as the export of India had increased due to the replacement of goods, which means the total output of India will increase. From the study, India exported US\$483 billion of goods and services (with services approximately 36% of the total [4]) with a rank of 13th (among 133 countries) [1]. India's exports have grown at an annual average of 1.6% while non-oil exports have grown at 2.8%, especially in the market of soybean, textiles, gems, and jewelry. Fortunately, by the statistics recorded at the end of 2019, the US-China trade war had brought India USD 755 million from additional exports, so the rising trend of economic growth and development is reasonable to be predicated to promote greatly [1]. This also benefits the balance of payments of India by fulfilling the huge gap of deficit using exports, or even better, leading to a trade surplus.

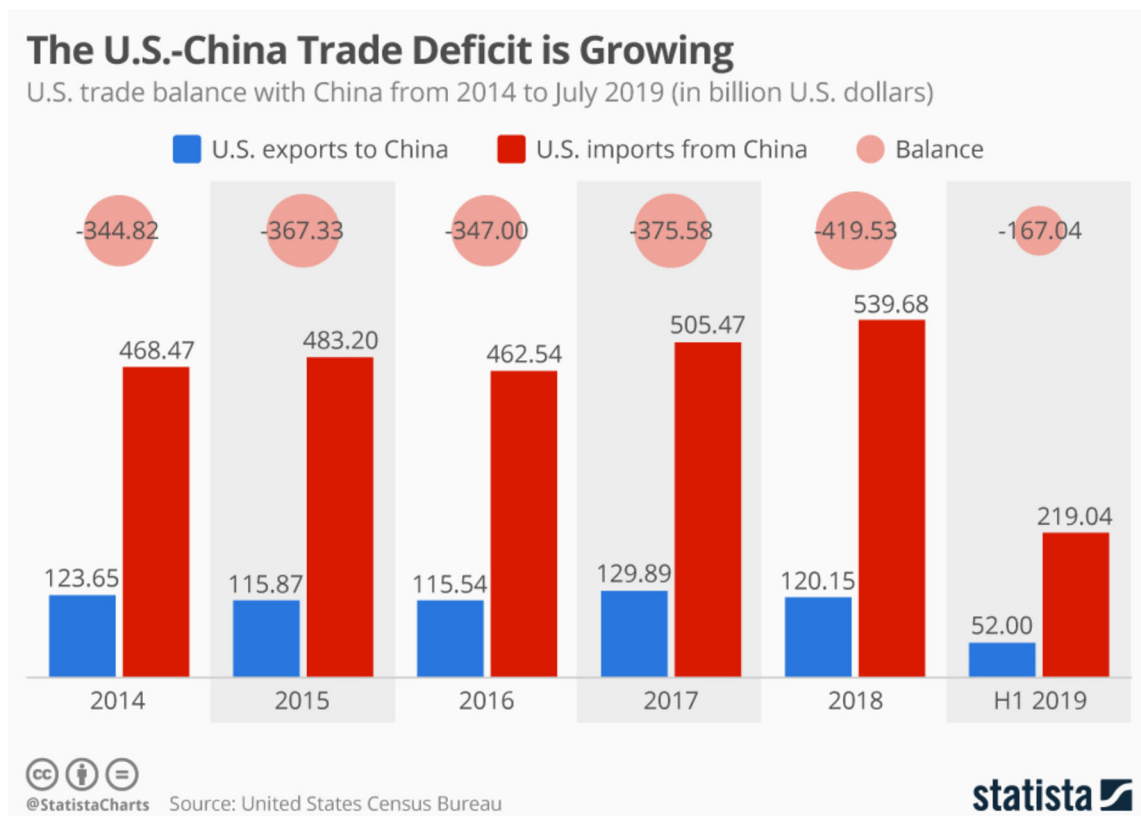


Fig. 1 U.S. trade balance with China [3]

To confirm these facts, Indian should be assessed and evaluated whether it can replace the position and function of China in the US market. The Finger–Kreininindex (FK), which is used to measure the similarities of export countries between countries, showed India is relatively capable to take the place of China. On the contrary, the figure is lower when it is measured between the US and India. Thus, this implies that India would find it harder to export to China those kinds of goods that the US used to export to China. Therefore, India should choose to export more to the US instead of China to maximize the benefit, because it could take more advantages in the US market due to the similarities between its export scheme and the Chinese export scheme.

3.2 Fear and Concern of other Economies

Besides the huge markers like the Chinese and the US, those trading partners of China or US markets would also be influenced by the trade war. Observing the harsh battle between the US and China, foreign investment may be afraid to enter the Chinese market because US sanctions or blocking of certain firms or industries in China are likely to result in great economic loss, which means it's going to be quite unstable, making the investors to lack of confidence. This situation is the same for some US companies as well. Under this substantial risk, to prevent possible loss, investors have to seek and find an alternate market with high similarities to China. Therefore, there will be some room for compensation and compliments in other countries, which is a nice opportunity in the whole global market. In this way, India could also grab a bit of the market share of the US and China, penetrating other countries markets. If India could form a long-term trading relationship with the US to replace China, it can ensure it would gain a lot during a certain period.

3.3 More Multinational Companies Involves, More Investment (Foreign Direct Investment)

What's more, since it's said in the previous few paragraphs, there will be some space for India to take more market share of the global from other countries' markets, which will improve the competitiveness of India. Due to the increase in competitiveness, India is likely to see a further increase in FDI following the recent change to FDI regulations [5], since the investors will be attracted

to India since they've seen the bright prospect of India: there are a lot of similarities between India today and China 30 years ago, such as the jumping GDP, the enormous size of the population, abundant resources. India even has lots of well-educated engineers which China did not have 30 years before. Moreover, India has a larger amount of educated and English-speak laborers with university degrees. Skilled laborers from India have become the hotties in Silicon Valley nowadays. FDI inflows from the U.S. in India rose by 65.38 percent to USD3.13 billion in 2018-19, in addition to inflows from China [5]. Venture investors cannot stop imagining the possibility of developing a fine technological research base with cheap skilled individuals living around. In the comparison of the average age of the population between India and China, India is 10 years old younger (28.4 compared with 38.4) which also means there is a more energetic labor force in India's market [6]. Young people tend to learn and accept new technology faster than elder ones. This means India's labor force tends to be more productive and has higher mobility than the labor force in China. From the image below, it's seen that the young ones (20-39years old) in India are much more than the young people in China [Fig. 2].

Population						Age Group			
Year	Population			Growth (%)		Age Group	China	India	China-India
	China	India	India-China	China	India				
2021	1,444,216,102	1,393,409,033	-50,807,069	0.34	0.97	00-04	82,445,544	117,805,565	-35,360,021
2020	1,439,323,774	1,380,004,385	-59,319,389	0.39	0.99	05-09	86,773,230	116,626,725	-29,853,495
2019	1,433,783,692	1,366,417,756	-67,365,936	0.43	1.02	10-14	84,896,388	124,776,306	-39,879,918
2018	1,427,647,789	1,352,642,283	-75,005,506	0.47	1.04	15-19	82,241,130	126,256,263	-44,015,133
2017	1,421,021,794	1,338,676,779	-82,345,015	0.49	1.07	20-24	85,794,296	123,110,514	-37,316,218
2016	1,414,049,353	1,324,517,250	-89,532,103	0.51	1.10	25-29	93,433,407	118,131,573	-24,698,166
2015	1,406,847,868	1,310,152,392	-96,695,476	0.53	1.12	30-34	126,667,892	113,106,958	13,560,934
2010	1,368,810,604	1,234,281,163	-134,529,441	0.56	1.36	35-39	105,660,611	105,283,718	376,893
2005	1,330,776,380	1,147,609,924	-183,166,456	0.58	1.59	40-44	94,048,289	92,386,031	1,662,258
2000	1,290,550,767	1,056,575,548	-233,975,219	0.71	1.78	45-49	115,401,864	81,016,434	34,385,430
1995	1,240,920,539	963,922,586	-276,997,953	0.89	1.94	50-54	124,872,825	70,233,679	54,639,146
1990	1,176,883,681	873,277,799	-303,605,882	1.6	2.10	55-59	103,608,816	60,353,210	43,255,606
1985	1,075,589,363	784,360,012	-291,229,351	1.65	2.29	60-64	79,097,558	49,909,068	29,188,490
1980	1,000,089,228	698,952,837	-301,136,391	1.42	2.34	65-69	74,765,216	39,432,294	35,332,922
1975	926,240,889	623,102,900	-303,137,989	1.96	2.35	70-74	48,884,701	25,435,500	23,449,201
1970	827,601,385	555,189,797	-272,411,588	2.68	2.23	75-79	27,725,241	15,511,044	12,214,197
1965	724,218,970	499,123,328	-225,095,642	2.25	2.10	80-84	16,535,272	8,782,263	7,753,009
1960	660,408,054	450,547,675	-209,860,379	1.57	1.98	85-89	8,094,794	3,809,953	4,284,841
1955	612,241,552	409,880,606	-202,360,946	1.52	1.81	90-94	2,647,698	1,142,537	1,505,161
1950	554,419,269	376,325,200	-178,094,069	-	-	95-99	539,846	248,124	291,722
						100+	81,484	51,274	30,210
						Total	1,444,216,102	1,393,409,033	50,807,069

Fig. 2 The comparison of the population between two countries [7]

These not only gave MNCs an image of great economic potential but also an image of development, leading them to tend to invest more in India. To attract those international capitalists or even further, make them stable investors and partners of India, India should also continue to use trade policy as a means to regulate domestic supply and to address short-term objectives such as containing inflation and fluctuations in commodity prices, giving the investors from other nations an idea of stability and confidence to persuade themselves to invest or open MNCs in India, since a country who has potential and also is not suffering from unstable and chaotic international disputes, especially with superpowers will be the first choice in front of the other which have high risks or in the center of the international conflicts.

3.4 Secondary Sector: Innovation and Efficiency

Those FDIs might alter the secondary sector in India significantly. The role of China in globalization is the manufacturer of the world. If India enables to capture enough financial aid and technical upgrades, it should achieve outstanding economic growth as China has done, or even better. Since more FDI flow into India, more entries of MNCs will bring innovative technology and methods of management/training into the country, making the industries more efficient to promote productivity.

It will also provide more job opportunities for labor in India, hopefully, can solve the problem of unemployment: in the short run, the promotions in the secondary sector create well-paid job opportunities, and more labor would be able to enter the market and contribute which would lead to higher output; in long run, it could lead to a manufacturable reform, which tends to drive up India's productive potential a lot. Better technology and more skilled workers can raise the aggregate supply of the economy, hence purchasing a long-term and more sustainable development of India, increasing the total output without significantly increasing the inflation rate.

3.5 Economic Development

Furthermore, economic development always comes along with economic growth. When India encounters a surplus in international trade, not only the profits from selling products would benefit firms and individuals but also the taxation on export would benefit the government. The government gains revenue from the export and could make beneficial use of it. For example, it can invest in social welfare, such as lots of social benefits. Moreover, India can improve the infrastructure so that the overall production costs may be reduced at a national level: if infrastructure improves, such as roads and highways, the transportation costs will decrease and the time for transportation will also decrease, which means the product will be more efficient and cheaper. Also, it can help with the redistribution of income, which is also a macroeconomic aim of the government, transferring the wealth from the rich to the poor. Investing in public goods can also be an effective way to allocate the taxation collected, especially on education and healthcare, which can improve HDI (Human development index), a criterion that measures the standard of living of Indian households calculated from three aspects: life expectancy, education, and income. Indian households' living standards may also be developed by receiving more disposable income due to a decrease in unemployment, which means the average income might rise and they can buy more to develop their quality of life.

All above are the most likely benefits that India could gain during this battle, but in reality, all of those need the Indian government's wise ideas and significant efforts to achieve so that it would not miss those good chances. India should make planning a precise, data-supported, logical research-based strategic trade policy a priority, including the impact of participation in plurilateral trade agreements. The decisions India made toward the trade war will affect the results of India in the trade war, such as how to set the tariff from the US and China's imports to India. If India tries to add more proportion of tariffs on the import of those superpowers, it's not only making itself into this hot-potato situation but also missing these opportunities for the country to develop.

4. Negative Effects

Although India is not the center of the trade war, it has also been negatively affected. The United States has imposed 25 percent tariffs on more than 800 countries to offset its \$375 billion trade deficit with China.

4.1 Costs: Inflation, Tariffs, and Declining Living Standard

Since the trade issues between the U.S. and China began, other countries such as India and Pakistan, are also affected. Every country has to get used to the frequently dynamic changes in economic and political aspects. Such changes could lead to shortages on the supply side and demand side. Prices of imported raw materials increase due to the tariff impositions, they likely drive up costs of production and eventually enforce consumers to pay a high price in the final good market, cost-push inflation may occur, lay-offs and unemployment, even recession could follow; prices of some final goods which could not be produced domestically also increase due to the tariff impositions, they could lead to a shortage in the market and reduce standards of living, social chaos could occur in some extreme cases. As a result, the increasing tax burden leads to soaring CPI and PPI. India has to pay about \$241 million in taxes to the United States due to the tariffs on steel and aluminum, and the number of taxes is expected to rise continuously [8]. As a response, India has increased its taxes rate on US exports

and its local tax rate. India however is much dependent on US production. It is unlikely enables to balance of the added tariffs by the US. In addition, India might have to implement a contractionary monetary policy in some extreme cases. Enforcing appreciation in currency helps the country to offset the negative effect of tariffs in the short run; yet such intervention harms the economy badly at the same time by weakening the competitiveness of its exported goods and services, which contracts its aggregate demand. Ultimately it makes life more difficult for Indian consumers, whose GDP per capita is expected to drop under the radiation of a trade war.

4.2 Indian Government Pressures

India's bad loan position makes multiple challenges and puts pressure on the face of its government. The loans could be separated into 2 parts: foreign aid and domestic debt. India's external debt stands at \$620 billion. The value of the rupee has fallen and even reached a low point. When on some occasions it was hovering around 79000 against the US dollar [Fig.3].



Fig. 3 the exchange rate between USD and INR [9]

This coincided with Donald Trump's threat to impose a new round of tariffs on \$200 billion worth of exports. This trend can be traced to the weakening of the US dollar. As this would automatically hurt India's trade deficit and cause a chain reaction of sorts. When the price of imported goods rises, it also raises domestic product prices, which leads to inflation. Continuous rising inflation will reduce demand and also affect people's savings. This will hurt the Indian economy as savings and investment are the main factors of economic growth [10]. As inflation rises, the Reserve Bank of India will raise interest rates and take necessary steps to control price rises [8]. That would increase the country's overall borrowing costs and shrink aggregate demand. As the rupee depreciates, the external debt burden of governments and companies rapidly extends.

All key indices of the stock market have taken a beating. Indian stock market during the China-US trade war fell due to the cautious attitude of investors. The BSE, Sensex, and NSE regularly plunge [8]. In this process, the Sensex still saw regular plunges and the Nifty's performance fell sharply, but now the Sensex is still trading below average at around 37,521 [8]. Moreover, the stock market always plays a crucial role in fund financing. A downward going trend in the stock market gives an unfavorable signal that investors are losing confidence in the market. Indian companies are being challenged to finance through IPOs. The undervalued blue chips have to undertake the prevention of hostile takeovers.

4.3 Supply Chain Disruption

Supply chain disruption is another imminent threat. China used to occupy 30% of manufactured imported goods of the United States, and China also contributes a sizable portion of Indian exports. Due to the relatively cheap labor and machinery in India, a large number of categories of needed intermediate materials by China are processed locally in India, and then these intermediate products are assembled into final products in China. If America's demand for Chinese exports falls, it will also directly affect the Indian market. Benefits of production would go, also job opportunities for low-skilled workers would go. Moreover, once such a scene appears, its economic loss cannot be measured by money, and a high unemployment rate will lead to social problems, such as crime rate, divorce rate, and drug abuse rate. Standards of living decline in India. On the other hand, this may lead to oversupply in emerging markets where these products are imported. India is one of these markets.

4.4 Impact on Expectations and Confidence

The instability of international political factors has led to the sluggish trend of the world economy. Such a trend in the US-China trade war will have a serious impact on expectations and confidence about the growth of the economy. Emerging countries over the world start to be concerned about who is next on the trade war list of the US.

First, protectionism starts becoming popular. Even a country such as India, which has become the fifth largest economy in the world, could be under threat made by the US one day. To prevent strategic sanction, the establishments of full industry chains are crucial before the next trade war comes. FDI in foreign countries turn out to be less favorable than local investments.

Second, the belief in comparative advantage theory starts to collapse. In the past decades, developed countries loved to transfer their secondary sector to developing countries to enjoy the low labor costs and cheap natural resources, which keep profitable margins from design and branding processes and protect their environmental conditions from production pollution. As a tariff is tagged on the geographical nation, the MNCs make production in China is negatively affected. Their CEOs might have gotten used to the feeling of being on pins and needles.

What's more, manufacturing sectors are going back to the developed countries if the costs of tariffs are outweighed the costs to quiet the protest interventions made by environmentalists. Without the help of transfer in technology, emerging countries like India would struggle in the way to complete their first stage of capital accumulation. It might take several more years to achieve their target urbanization rate due to the reduction in FDI reducing job opportunities in cities.

Furthermore, the skilled labor emigration trend could occur. In India, individuals have observed what happened to China and what happened in Japan 40 years ago. Some well-educated individuals might choose to move to developed countries, such as the US, to elude the negative effects caused by economic and political uncertainty. Those elites utilized the best educational resources in India. They are extremely productive, and they could easily get high-paid jobs in a developed country and enjoy higher levels of living standards with their families. However, such an emigration trend would thump India through its losses in human capital.

4.5 Cultural Impact

The problems of gender inequalities frequently occur in India. Less women go out to work, which is a great loss of the labor force. It is well-known that women can contribute a sizable proportion of production nowadays, however in India, they hardly ever get a chance for a formal occupation. This reduces the productivity potential of India. The issue of the caste system, it's the same as gender inequality. People are divided into levels by caste system, and only the upper class were the ones who can enjoy nice education. It restricted the level of education and limited the opportunities for job people can get, which then influenced the productivity potential of India.

5. Summary

To evaluate, India ideally looks like a perfect substitute to replace China to become the next factory of the world. The suitable average age and skill-labor population in India are the favorable elements to attract FDIs. If India does enable to absorb part of the manufacturing sector from China, another leap would show in its GDP. However, some things restrict the economic growth of India. Though India has a large number of high-skilled laborers in computer science and engineering aspects, the problems in the country still confuse a lot of MNCs and foreign investors when making investment decisions. In conclusion, India has the chance to be the second 'China'. An introduction of wise government intervention, if there is any, would help this country to achieve the next step much easier.

References

- [1] PTI, New Delhi, US-China Trade War Effect! India Gains \$755 Million from Additional Exports. Business Today, 2019.
- [2] Jodie Miller, US US-Chinaade War Effect on Global Economy, 2020.
- [3] Katharina Buchholz, the US-China trade deficit is growing, August 19, 2019.
- [4] Chadha Rajesh, Pohit Sanjib and Pratap Devender. THE US-CHINA TRADE WAR: IMPACT ON INDIA AND ITS POLICY CHOICES, 2019.
- [5] Neeraj Bansal, Impact of U.S.-China Trade War on India, ASEAN Countries. KPMG, 2020.
- [6] Zhang Chenghui, Comparison of India and China's population, 2022.
- [7] Comparing China and India by Population - StatisticsTimes.com. Statisticstimes.com, 2020
- [8] US and China Trade War Impact on India. Finance, Tech & Analytics Career Resources | Imarticus Blog, 2018.
- [9] USD-Indian rupee exchange rate graph_Real-time analysis of today's market trend_Investing.com.n.d.Investing.com.Accessed November 6, 2022
- [10] Monday, Rohit. n.d. Explained: What a Weak Rupee Means to the Indian Economy | Policy Circle. Accessed November 6, 2022.