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The Impact of the Trade War Between China and the U.S. on the Economy of Indonesia

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Abstract

China-US Trade War is an International Trade situation where two of the most powerful economic country increasing their tariff for trading goods to each other. The War itself actually occur for a long time but not as escalated as of 2018 which was started by the US itself and its current President, Donald Trump. Many people concern that this war may affect the world economy development since both of the countries are being the source of trading for many countries. This paper will discuss about how The China-US Trade War can influence Indonesia Economics which will bring either opportunity or problem. Research in this paper discusses about Indonesian Economy ranging from exports, imports, exchange rates and FDI which may be affected by Trade War using Correlation Test as research methods.

Keywords: International Trade, China-US Trade War, Export, Import, FDI, Exchange Rates, a, Indonesia Economic

Introduction

Based on historical report, the history repeats itself. That in fact liberalization which has been pushed up by developed countries is actually very strong in their nuances of unilateral interests (Firmansyah et al., 2022). So, when trade liberalization is felt to benefit developed countries, it will be encouraged as much as possible. But when it was felt that it had become increasingly unprofitable, he would turn around, and become an opponent of liberalization (Pradhan et al., 2014).

Since the campaign period his presidency, US President Donald Trump has indicated will direct the economy US to protectionism (Anggraini & Widarjo, 2020). Thing the more visible with worsening economic relations US-China that leads to trade war (Agusalim & Pohan, 2018). The existence of a trade war between the United States and China began when Donald Trump as the president of the United States asked the ministry of trade, to increase tariffs on imported goods from China (McNair, 2017). Many parties consider that this effort is a manifestation of Trump's political promise, "to make America great again". And the promise is implemented, of course by increasing foreign import tariffs. One of them is China (Dimmock et al., 2021).

Government President Donald Trump is wearing import tariff of US $ 50-US $ 60 billion for a number of Chinese products who entered America in efforts to improve the economy domestic nature and reduce the trade balance deficit between the two countries. President Trump announced increase import tariffs by 15% for steel and 10%

for aluminum. In addition to imposing import tariffs, the US also plans to limit investment and take action for China in the World Trade Organization (WTO) because they consider the country it is being unfair inside bilateral trade. Government China countered US actions with increase import tariffs by 25% against US imported products and will bring this problem to the WTO too (Pitoyo et al., 2020).

At the global level, trade wars within these two influential countries which is the two biggest economic in the world, can triggered the weakening of many country economy like EU, UK, Hongkong, even the world economy (Odoh & Nwibo, 2017). WTO Director General Roberto Azevedo said the WTO was experiencing one of its toughest periods because there was a risk that a trade war would cause a decline in global economic growth (Meyer & Shera, 2017);(Hidayat et al., 2024). Azevedo's comments are in line with the increasing trade tensions between the US and China, marked by the implementation of import tariffs between the two countries.

President Donald Trump's policy of implementing import tariffs can backfire for the US. China is not the only country that has been threatened by the suspension of tariffs on imports of steel and aluminum. Although it was finally canceled, President Trump also directed his policy to his main trading partners in the European Union, Argentina, Australia, Brazil, Canada, Mexico and South Korea until May 1, 2018. Instead of gaining profits, the US will get opposition from countries others who responded also with the new import tariff policy.

US President Donald Trump's protectionist policy triggered Indonesia's vigilance because of its impact on the world economy. Indonesia has expressed its readiness to retaliate if US President Donald Trump applies protectionist policies to Indonesian products. Indonesia’s Vice President Jusuf Kalla stated that if Indonesian palm oil was prevented from entering America, Indonesia would reduce imports of agricultural products from soybeans, corn and wheat from the US. In addition, Indonesia will also reduce the purchase of US-made aircraft.

Previous research by Carvalho (2019) We evaluate the impact of the US–China trade war using a dynamic computable general equilibrium (CGE) model of global trade. We conduct ex ante simulation analysis exploring three scenarios to understand how the trade war affects import tariffs, investment, and productivity. The escalation of the trade war reduces gross domestic product (GDP) in China and the USA by −1.41% and −1.35%, respectively. The trade war reduces nearly all sectoral imports and outputs in both countries. To reflect the important role of global value chains (GVCs), we modify the dynamic CGE model with agent-specific import demands, and we explore the difference between the results for the two models relating to the trade war impacts on GDP and bilateral trade. When GVCs are accounted for, the negative impacts on bilateral trade are more widespread across countries, and world GDP in the modified model is reduced by −$US450 billion. These results suggest that the GVCs play substantial role in determining trade responses at the disaggregated level.

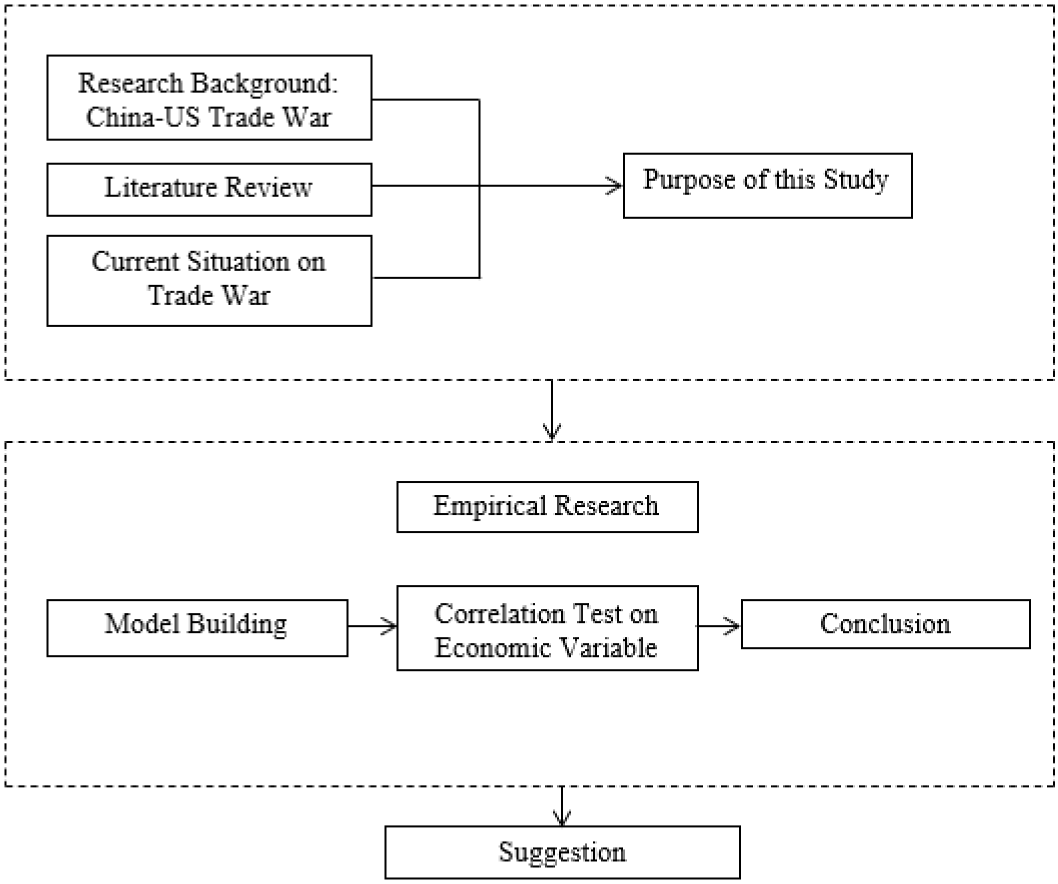
This study will discuss the relevance of trade war with economic growth in Indonesia (Danzer & Dietz, 2018). The current trade war will affect Chinese or American exports and imports. Economic growth is usually measured by looking at the GDP of a country. GDP itself is significantly affected by a country's export and import activities. Therefor the author will examine whether there is a significant impact between the situation of Indonesia's exports and imports and the situation of China's or US export imports that represent trade war.

Research Methods

The research method that will be used is the correlation method. The correlation method chosen in this study was due to the large number of dependent variables to be tested. Actually, the regression model can be used in this study, but because of the large number of dependent variables the regression is not suitable for this study. Program that will be used to conduct this research is Microsoft Excel.

The variables that will be used in this study are divided into two types, namely dependent and independent variables. Independent variable is a variable that is not affected by anything, in this case it is a variable that can represent trade war namely American exports to China, American imports from China, Net exports between China and America, and the exchange rate between American Dollar and Chinese Yuan. The dependent variable is the variable that will be influenced by the independent variable, in this case is the variable that can represent the Indonesian economy, namely Indonesia's exports and imports, FDI in Indonesia, and the exchange rate of the Indonesian Rupiah and US Dollar.

The type of data used in this study is secondary data that is quantitative, which means that all data variables to be examined are in the form of numbers. These data are obtained from the results of research, reports and academic reviews conducted by parties who have the competence to present the data, namely government institutions (www.bi.go.id, www.bps.go.id, www.kemendag.go. id). Data obtained in the amount of Indonesian Rupiah has been converted using the exchange rate determined when the data was obtained. The data used is data in the last five years and in quarterly form.



Results and Discussion

Analysis of the Current Trade War Situation

Trade War on US, China, and Other Countries

Either the agreement was made or not, but the US-China trade war has hurt the world economy. China's export orders slipped as European manufacturing weakened. The combined effect of a stronger dollar and a weaker yuan has also contributed to slowing growth outside the US and China. A trade war is likely to cause lasting damage to the world economy. Economists predict that reciprocal tariffs by the US and China can greatly influence the growth of the world economy, and there is evidence that is happening (Chand et al., 2017).

As explained in the theory above, trade also affects economic growth as measured by how much GDP growth a country has. The existence of a trade war caused trade between the two countries with the largest economy to be disrupted. Trade war affects the demand for goods from each country. With the weakening demand for these two countries, the level of exports is predicted to decline and weaken trade conditions. The weakening of the trading conditions also caused a weakening of manufacturing in a country. China, whose manufacturing index shows a decline, has caused other countries to supply raw materials for China to weaken.

In terms of international trade, China's exports and imports are actually still growing in a positive measure. During the period of January-August 2018, Chinese

exports were still able to grow at an average rate of 14% on an annual basis (year-on-year / YoY), while imports also continued to rise at an average rate of 21% YoY.
When Uncle Sam's import demand declined due to rising import tariff (imported goods will become more expensive), manufacturers in China will automatically reduce their production. When the slowdown occurred, China's economic growth was at stake.

China's Caixing Manufacturing PMI index continued to show a decline after passing the first semester of 2018. This index indicates the overall picture of manufacturing sector activity. When the PMI index is below 50 it means the manufacturing economy has contracted, whereas a value above 50 indicates expansion. In June, this index was able to stabilize at the level of 51.1. However, a month after this index fell to level 51, and continued to decline to touch the level of 50.6 in August 2018. July's reading was still lower than the market consensus at 50.7, while touching the lowest position since June 2017. This means that the processing industry activities in China are still expanding, but the pace has slowed significantly.

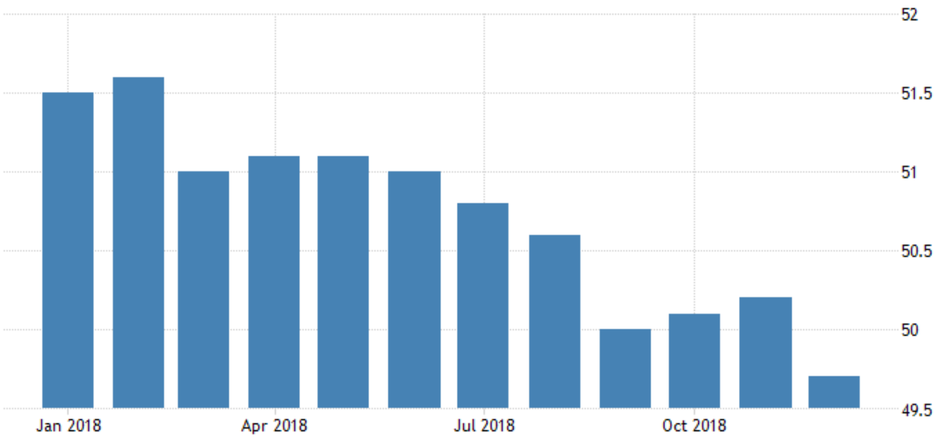


Figure 1. China 2018 PMI
Source: Trading Economics Website

China's economic growth also weakened. China's economic growth in 2018 was recorded at 6.6%. This growth is the weakest growth since 1990, the last 28 years. this condition is clearly inseparable from trade war. To see more clearly economic growth in the third quarter was recorded at 6.7% with a ratio of 6.8% in the second quarter. In the fourth quarter growth was recorded at 6.5% far compared to before the trade war, namely during the second quarter recorded on 6.8%.

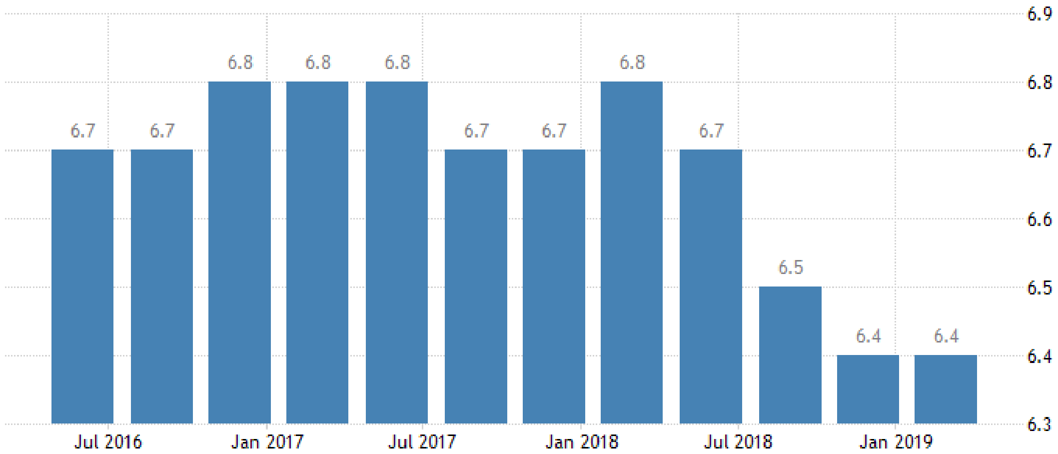


Figure 2. China Annual GDP Growth Rate
Source: Trading Economics Website | National Bureau of Statistics of China

The slowdown in China's economy then spread to other countries, especially in countries that are the main trading partners of China. The reason is, when China's industrial activities slow down, it means that demand for imports of raw materials / capital goods will decline. Or in other words, the demand for Chinese imports will also reduce. As in the case of China which reduced industrial production when demand for imports from the US declined (due to import duties), China's trading partners would eventually cut production of their goods due to reducing demand for Chinese imports.

Based on data from the UN Comtrade, China's main trading partners (for import matters) are South Korea and Japan. In 2017, China imported goods from Japan and South Korea, amounting to US $ 165.79 billion and US $ 177.55 respectively. The import value is the highest compared to other countries. The two countries also turned out to have contracted the "virus" of the US-China trade war. Although not as bad as what China experienced, the symptoms began to appear.

The Japanese Manufacturing Purchasing Manager Index (PMI) index fell to 52.3 in July 2018. The achievement was the weakest in August 2017. With the slowdown in the Japanese Manufacturing PMI index, Japanese industrial production also contracted by 0.9% YoY in June 2018. That growth was late in 1.5 years or since October 2016.

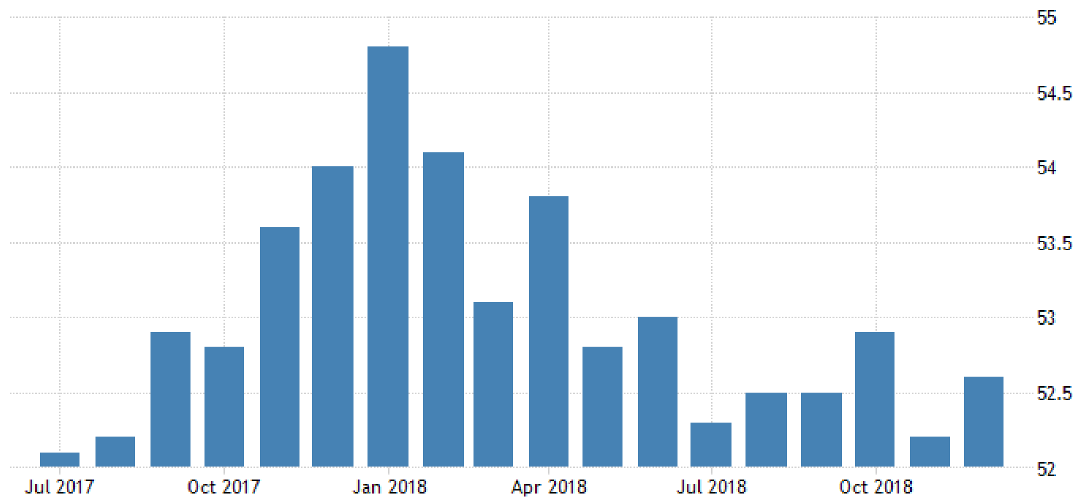


Figure 3. Japan 2017 – 2018 PMI
Source: Trading Economics Website

The situation in South Korea is not much different. After being able to hold above level 50 in the period January-February 2018, the South Korean Manufacturing PMI index fell back to the brink of contraction (values below 50) since March 2018. In July 2018, this index even touched the level of 48.3, which to be the lowest record in 1.5 years or since November 2016. The data above then shows that in fact Japan and South Korea are also beginning to be affected by the increasingly tense trade war.

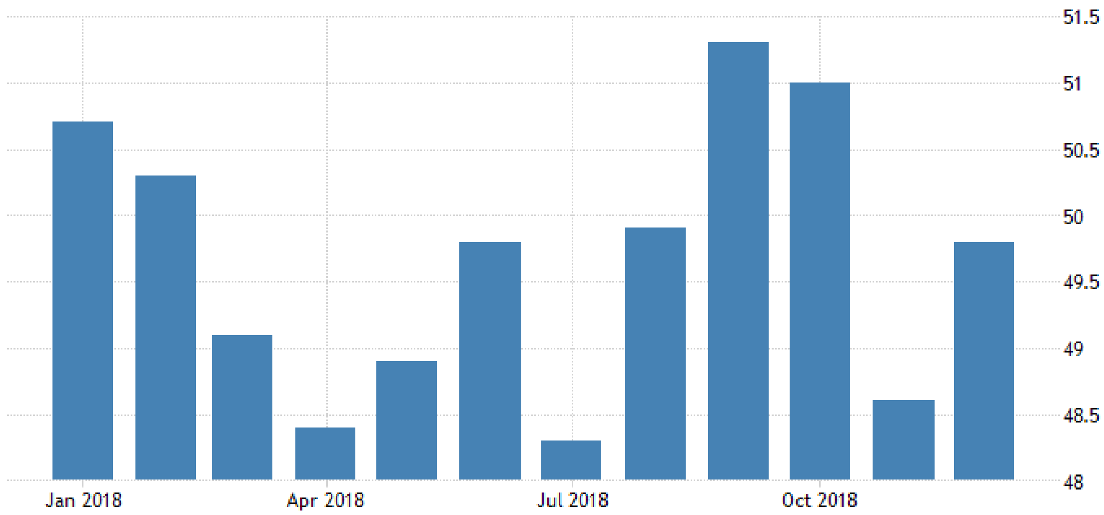


Figure 4. South Korea 2018 PMI
Source: Trading Economics Website

If more massive new import duties are executed, the economic slowdown of the two Asian countries can get worse. In fact, it is not impossible that the "virus" of trade wars finally spread to other countries, including Indonesia. Because, Japan, South Korea, and China, are the main export destinations of Indonesia.

The trade war started by the US began to hit the US itself, the most obvious example being Apple. The weakening of Apple Inc. sales became the clearest sign that President Donald Trump's policy of rearranging world trade turned out to have a negative impact on the US domestic industry. The trade war has threatened the Chinese economy which has grown rapidly over the past decade, which has increased the purchasing power of Chinese people and has invited aggressive global companies to target the markets of the world's second largest economy. The sharp decline in China's economic growth will cut US corporate profits. The US PMI also recorded a decline since July 2018, although it had experienced an increase in September and October this increase was still far compared to May 2018 and still experiencing a decline.

Investment Amidst Trade War

The China-United States (US) trade war provides an opportunity for Indonesia to become a place for investors who want to leave the two countries. Investors in China are afraid and start counting in running their businesses because they will be hit by the import duty tariff war applied by the two countries. Thus, the opportunity for relocation has been anticipated by developing countries in Asia, one of which is Indonesia. For example, the iPhone component builder from Taiwan, Pegatron will transfer part of its production from China to Indonesia. The transfer of production is caused by a trade war between the United States (US) and China.

Taiwanese manufacturers will divert non-iPhone production exposed to US tariffs on Chinese exports. Pegatron moves non-iPhone production bases to avoid high tariffs when products are exported to the United States. Trade war keeps producers crushed due to rising wages and reduced workforce. While the production costs are getting higher. Despite the opportunity and example in terms of investment, the value of investments entering Indonesia is not high in the third quarter and fourth quarter of 2018 compared to the previous year. This is believed to be affected by a trade war in which investors are still taking steps to be cautious, preferring to wait and see. Phenomena can also be felt by other countries throughout the world.

Indonesia on Trade War

The economic slowdown caused by the trade war has also troubled Indonesia, moreover the US and China are experiencing a slowdown which in fact is Indonesia's biggest export destination. At present, what Indonesia is worried about is the situation in China. The economic slowdown in China is feared to affect the demand for exports from Indonesia, one of the largest expos from Indonesia, namely raw materials in the form of coal for Chinese manufacturers.

The Ministry of Energy and Mineral Resources noted exports to China until August 2018 still dominated. As a result, the benchmark coal price will still be influenced by the Chinese market (Safitriani, 2014). According to data from the Ministry of Energy and Mineral Resources, coal exports as of August 2018 were aimed at the Chinese market reaching 44.5 million tons or around 31% of the total exports of Indonesian coal exports in the period. As a result, China's impact on reducing demand greatly impacts the benchmark coal price.

Another thing that is feared is that Chinese goods are oversupplied due to declining demand from the US will flood the Indonesian market and cause competition with local products (Purwohandoko & Akbar, 2018). Vice versa with US, goods that cannot be exported to China from the US due to reduced demand are feared to flood the Indonesian market, although not as much as Chinese products scale. For new market opportunities in China and America and the opportunity for foreign investment to enter, Indonesia must compete with other ASEAN countries which are targeted by investors amid the warming of trade wars.

In this case, if seen from investment, Indonesia is still unable to compete with other countries, and for the quality of goods Indonesia also still has shortages for certain goods if compared with neighboring countries (Chu, 2018). One example of a new market that Indonesia is currently getting is steel exports to America. The US, which recently imposed a new steel tariff on China, turned to Indonesia to buy steel. Steel that is usually imported from China is expensive because of the tariffs and Americans are looking for alternatives to China.

Conclusion

The Results from test conducted above shows that Trade War has minor influence on Indonesian Economics, the influence may be indirect influence to Indonesian Economic. Even so, Indonesia still has to be vigilance about the Influence since it has a moderate level of correlation with variables that represent Trade War. The Influence from Trade War may not be or cannot be seen in a short term, but given the influence is indirect influence, the effect may can be seen in a long term as the Trade War still occur. Indonesia should make anticipation and some new policy to hold and overcome the effect of Trade War.

From the results above it can be concluded that, the trade war variable that affects Indonesia is US imports from China or it can also be called Chinese Export to US. This variable most influences Indonesia's exports and imports, so the policy that will be made must focus on these two factors, namely Indonesian exports and imports. Another thing that greatly affects the trade war and also the Indonesian economy is the value of currency exchange, which also at this time The Feds raises the US Dollar interest rate. This also has an impact on trade prices which will affect the amount of exports and imports. Not only US and China are affected by this phenomenon, Indonesian Trade is also affected by rising US Dollar interest rates.

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