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## The Impact of US-China Trade War on South Korea's Economy

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### **Abstract:**

*This study analyzes the impact of US-China trade war on South Korea's economy. The U.S.-China trade war began in 2018 when the U.S. President signed an executive order that imposed high-rate tariffs on Chinese products. The trade war between the two countries later expanded to technical issues due to the U.S. sanctions on Huawei and China's suggestion of restricting exports of rare earths, and spread to the regime when the U.S. Department of Defense stated Taiwan as a country, breaking the "One China" principle. South Korea has been affected tremendously with the degree of US-China trade war. Thus, this research investigates how South Korea is affected economically in detail. This study takes in count of several events in Korea after the US-China trade war. The analysis of this study clearly shows following the trade war, South Korea's economic status shows negative outcomes; in other words, US-China trade war results in pessimistic consequences.*

**Keywords:** US, China, trade war, South Korea, economy

### **1. Introduction**

The trade war between the U.S. and China, which continues from 2018 to 2019. The U.S.-China trade war began in March 2018 when U.S. President Donald Trump signed an executive order that can impose high-rate tariffs on Chinese products. The trade war between the two countries, which began with tariffs, later expanded to technical issues due to the U.S. sanctions on Huawei and China's suggestion of restricting exports of rare earths, and spread to the regime when the U.S. Department of Defense stated Taiwan as a country in a report released in June 2019, breaking the "One China" principle. But the conflict between the two countries first came to an end when the leaders of the U.S. and China agreed to a cease-fire at the G20 summit in Osaka, Japan, on June 29, 2019.

The U.S. began a trade war on July 6, 2018, imposing 25 percent tariffs on 818 Chinese goods worth 34 billion U.S. dollars. In response, China immediately responded by imposing tariffs on 545 items, including agricultural products and automobiles, and brought the U.S. to the World Trade Organization. As China responded, the U.S. announced on July 10 that it would impose 10 percent tariffs on a separate \$200 billion worth of imports as a means of re-rehabilitation. Later on, Aug. 23, the two countries imposed additional tariffs on goods from each other worth an additional 16 billion U.S. dollars. On Sept. 24, the U.S. imposed a 10 percent tariff on the size of \$200 billion worth of Chinese imports, while China also imposed tariffs of up to 10 percent (5-10 percent) on products worth \$60 billion, including U.S. meat and chemical products.

South Korea is in a situation where it cannot be reassured. The United States and China are South Korea's first and second-largest exporters. British analyst Pixet Asset Management ranked South Korea sixth after analyzing the country most affected by the U.S.-China trade war. The combined value-added exports and imports accounted for 62.1 percent of the country's economy. It was the headline newspaper when I first saw the issue. I've never seen a trade war this big before, and it was certain that this kind of conflict would affect not only South Korea but also the world. It was definitely a concern because a few issues were emerging that South Korea's economy, usually companies, was being effected and that huge negative consequences might be the results. I have always been interested in economics, especially this type of economic issues related to global affairs. My interest grew day after day, and I finally decided to write a research paper about this topic to understand deeper about the US-China trade war and the effects to my country, South Korea. This study will research and take a deep understanding of several representative examples of the effects of US-China trade war on South Korea's economy. Also, this study will quote experts on this U.S.-China trade war to find out what the outlook is and what impact it will have on South Korea in the future.

### **2. KIEP: Korea's Exports Expected to Fall by \$5.2 Billion**

An analysis by a state-run think tank showed that South Korea's exports to the two countries will drop by about \$5.2 billion if plans to impose additional tariffs by the United States and China are fully implemented. Starting from Feb 2019, U.S. has begun levying 15 percent tariffs on \$112 billion worth of imports from China, out of the \$300 billion worth of imports from China that it has decided to impose additional tariffs. China has also counterattacked. The Chinese

government immediately announced that it would impose an additional 5-10 percent tariff on 5,078 U.S. imports and \$75 billion worth of imports. The KIEP estimated that if tariffs are imposed at this rate, South Korea's exports to the two countries will fall by \$5.22 billion. The damages were derived from direct effects leading to reduction of U.S.-China exports and imports, reduction of U.S.-China production, reduction of Korean intermediate goods exports, indirect effects such as reduction of U.S.-China growth, and reduction of demand for imports to Korea.

Specifically, the KIEP forecast that the tariff, which has already taken effect, will expand the U.S. exports to China by \$20.2 billion and China's exports to the U.S. by \$67.3 billion, respectively, and to \$25.6 billion and \$120.8 billion if measures to take effect in the future are included.

Based on the analysis, the KIEP predicted that South Korea's exports to the United States will fall by a total of \$910 million, or \$140 million in direct and indirect effects of \$770 million.

Korea's exports to China will shrink by 4.31 billion dollars (direct effect \$2.62 billion, indirect effect \$1.69 billion).

(units: billion \$)

	1 <sup>st</sup> ~ 3 <sup>rd</sup> Action Effect			4 <sup>th</sup> ~ 6 <sup>th</sup> Action Effect		
	Direct Effect	Indirect Effect	Total Effect	Direct Effect	Indirect Effect	Total Effect
Korea's Decreased Export to the U.S (rate).	1.0 (0.1%)	4.3 (0.6%)	5.3 (0.8%)	1.4 (0.2%)	7.7 (1.1%)	9.1 (1.3%)
Korea's Decreased Export to China (rate)	13.4 (0.9%)	11.4 (0.8%)	24.8 (1.6%)	26.2 (1.6%)	16.9 (1.1%)	43.1 (2.8%)

Table 1

According to industries, exports to the U.S. will be hit hard by cars, trailers, computers, electronics and optical devices, and exports to China will be hit hard by computers, electronics and optical devices.

So far, South Korea's market share in the U.S. import market has risen slightly as the U.S. has imposed additional tariffs on Chinese products. However, the KIEP estimated that Korean products did not have much reflexes in the Chinese import market, replacing American ones.

"The U.S. and China are trying to reach a conclusion through additional negotiations, but the possibility of a settlement has become smaller as the U.S. designated China as a currency manipulator," the KIEP said. "Even if there is progress in negotiations, there is a possibility that the conflict will continue until next year's U.S. presidential election."

### 3. IMF World Economic Outlook Report

South Korea is the most vulnerable country to higher tariffs following the U.S.-China trade war, the International Monetary Fund warned. If tariffs go up, China's exports to the U.S. will decrease, and Korea's exports to China will be directly hit by the drop in the electricity and electronics sectors, including semiconductors. Such an IMF diagnosis means that the government should speed up policies to diversify export markets and boost domestic demand, experts here interpreted.

In its April 19 World Economic Outlook Report, the IMF estimated that a 1 percentage point increase in global tariff rates would reduce Korea's GDP by 0.65 percentage point. Of the nine countries analyzed by the IMF, South Korea's GDP decline was the largest. Germany (0.48 percent) followed, followed by Japan (0.33 percent) and China (0.27 percent). (units: %)

Effect of a 1% Increase in Global Tariff Rates on GDP			
South Korea	-0.65	Italy	-0.19
Germany	-0.48	United Kingdom	-0.19
Japan	-0.33	France	-0.15
China	-0.27	United States	-0.13

Table 2

The IMF explained that the negative effect of Korea and Germany, which are highly integrated through the global supply chain (a series of processes in which companies purchase raw materials, process and sell them to create value added), was largely attributed to Korea and Germany.

"Although there are many global value chains (supply networks) in electricity and electronics at the center of China, the recent slowdown in Korea's semiconductor exports to the U.S. was due to the decrease in China's exports to China," said Song Young-Kwan, a researcher at the Korea Development Institute. Song analyzed, "Germany, like Korea, has

a high proportion of exports in GDP, and thus is more affected than Japan and China, which account for less than 20 percent of exports."

However, a government official cautioned against further interpretation, given that the portion of non-tariff barriers such as delayed customs clearance is growing in comparison with tariffs. In its report, the IMF also presupposed that the impact of tariffs on global trade has decreased, a government official stressed. Yet, Korea cannot be free from the effects of the trade war between the U.S. and China, which include raising tariffs and strengthening non-tariff barriers. The IMF report suggests the need to diversify export markets and implement policies to expand domestic demand, experts interpreted.

If the U.S. imposes 25 percent tariffs on all imports from China and China imposes the same retaliatory tariffs on all imports from the U.S., the impact will be mixed.

South Korea's exports to the U.S. will increase 7.7 to 10.3 percent in the long term, while those to China will fall 1.3 to 5.3 percent, the IMF estimated. Because amount of goods exported from China to the U.S. is decreasing, South Korean products are imported to the U.S. due to 'export conversion effect'. U.S. and Chinese GDP were estimated to fall 0.3 to 0.6 percent and 0.5 to 1.5 percent, respectively.

#### 4. Korean Companies Forced to Choose in the U.S.-China Trade War

Between the U.S. and China, which are waging a trade war, Korean companies are increasingly in a difficult position to choose either. China's National Development and Reform Commission, the Commerce Ministry and the Ministry of Industrial Information Technology have called in major global technology companies and warned that they will face serious consequences if they stop supplying parts to Chinese companies as required by the Trump administration. Companies that were called to the Chinese authorities included Microsoft and Dell of the U.S. and ARM, a British semiconductor design company, as well as South Korea's Samsung and SK Hynix.

If Samsung and others accept the U.S. government's demand and cut off the supply of parts to Huawei, they could be blacklisted by China's commerce ministry and sanctioned. Samsung Electronics and SK Hynix could be hit hard if their relations with China are strained. For Samsung Electronics, Huawei is one of the top five customers. While competing with Huawei in the smartphone sector, Samsung is supplying semiconductors and displays to the company. These companies want to continue to do business in China, a huge market, but they cannot help but be wary of the U.S.

An unnamed company official declined to comment directly on reports that the Chinese government warned global companies in a phone call with Yonhap News Agency, but said, "Somehow, we are in a very difficult situation. Samsung and SK Hynix are already under investigation for anti-trust in China. They are worried that the results of the anti-trust investigation will be affected depending on the pattern of the development of the trade war.

The National Market Supervision and Management Bureau is conducting an anti-trust investigation into the three companies: Samsung Electronics, SK Hynix Inc, and Micron of the United States. The three companies have more than 95 percent of the memory chip market, including DRAM, and they are suspected of abusing their monopolistic status to sell their products at high prices.

A Chinese foreign ministry official met with South Korean reporters visiting Beijing and said South Korea should make the right judgment amid the U.S.-China trade war. He then argued that the South Korea-China relationship could face difficulties depending on the judgment of the South Korean government or companies. The remarks were directly aimed at the U.S. Commerce Department's request to its allies, including South Korea, not to do business with Huawei after putting Huawei on a list of companies that have restricted transactions, citing security issues.

Some worry that Korea could suffer damage from the U.S. and China in the middle of a power struggle like the THAAD crisis. Some experts predict that the world will be divided into two economic blocs due to the cold war on technology, while diagnosing the current rising level of conflict between the U.S. and China as a technical war.

#### 5. Conclusion

As the study offers above, we can clearly see that the US-China trade war has an overall negative effect to South Korea's economy. Starting with the KIEP's insight of estimating Korea's export to decline by 5.2 billion dollars, the IMF World Economic Outlook report and the issue about Korean companies being in an ambiguous situation all adds up to difficult dilemmas. Through this research, one was able to look in depth of the issues surrounding the trade war and connect it to the expectations of South Korea. Some experts predict the trade war will end soon. However, whether the war ends or not, countries all around the world, including South Korea, will have to adjust to the new circumstances.

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