34th Asian Shadow Financial Regulatory Committee Statement

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Trade Wars and Their Effect on Asian Market Stability

While history has shown that no-one benefits from a trade war, it is important to understand the driving forces behind the current trade wars instigated by the United States of America, the most significant of these being against China. The US has large and persistent trade deficits with several countries, including Mexico, Germany and Japan, the largest being with China. It should be noted, however, that in a world of global supply chains and multi-national corporations with production in multiple locations, true sources of deficits are often hard to determine.

While the US recognizes that competition is at the heart of fair trade, it contends the playing field is not level, often to its disadvantage. In many countries, including China, market access for US companies and products are restricted while access to the US market is far less restrictive for these countries. Further, the US claims that these foreign markets have not protected intellectual property rights and even violated US trade sanctions. Although the US understands there will be no winners in a trade war, it believes that it would lose less because its market power will force rivals to finally yield to its extreme pressure, including sanctions, even if these are against WTO rules.

The disruptive impact on global supply chains has already caused many foreign companies to move (or plan to move) out of China, primarily into Southeast Asia, Vietnam in particular. However, these countries, which also have trade surpluses with the US, may themselves become US targets in the future. Just how large the full impact of these disruptions will be will depend on whether the trade war persists. Furthermore, there have been claims out of the US that Europe, Japan and in particular China are resorting to monetary and currency measures to counter US tariffs. Such claims, if true, can have serious implications for global financial market stability and eventually, slow down world growth.

Recent meetings at the G20 appear to have eased such tensions. Since then China has responded with a series of steps to end ownership limits for overseas investors in the financial sector, including banking, by 2020, a year ahead of schedule. These steps also included opening up its manufacturing sector and reducing its negative investment list; abolishing ownership limits in the securities, futures and insurance sectors; and not resorting to competitive currency devaluation. In addition, the Chinese have agreed to purchase more US agricultural products.

What is more worrisome is whether the recent escalation in tensions is a sign that the US initiated trade war is changing irrevocably into a permanent rivalry beyond trade, and into – at least for now, a technology war in the name of national security considerations. In this context, it is clear that US and Chinese interests are not compatible. The US approach using nationalism, appears to be unfortunate. In the current sentiment-driven environment involving trade tensions, this further adds to unwind the globalization of innovation and the technological development of the past thirty years. This could possibly be the beginning of a long-term decoupling into a two-sided global technological economy: each block viable without the other and each increasingly spinning in its own orbit. Surely, such a forced dichotomy is sub-optimal and even potentially dangerous.

Recommendations

1 WTO reforms are urgently required that take into account the need for fair trade practices, including the role of government-owned enterprises; due regard to intellectual property rights; a comprehensive system to account for environmentally responsible behaviour; and the future role (and definition) of emerging economies as well as regional and bilateral arrangements. In addition there needs to be strong and enforceable penalties for avoidance and infringement of its rules.

2 In the current environment of destabilizing trade tensions, the role of the BIS and IMF should be enhanced to regularly monitor their impact on monetary stability and financial markets, especially on global growth. In this regard, consideration should be given to the establishment of a formal Asian arrangement to monitor and assess the impact on Asia, in particular its financial markets, and recommend solutions to mitigate any adverse effects. This is vital because the current tensions exert a more than proportional impact on Asia in an environment where its financial markets are less mature.

3 Asia's export oriented economies result in persistent trade surpluses, often leading to balance of payments surpluses, which in today's context, is unsustainable. Hence the need for surplus nations to undertake structural reforms towards higher domestic consumption and to avoid trade conflicts and possible tariff barriers, and competitive currency devaluation. The international monetary system requires greater balance in trade and payments without undue reliance on a dominant reserve currency. Current trade sanctions and tensions point towards the need for better coordinated international efforts for currency and monetary arrangements to help maintain stability in global payments and international financial markets.