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TRADE WAR AND THEIR IMPACT ON INDIAN FINANCIAL MARKETS

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ABSTRACT
Emerging markets, especially India, are being impacted by global trade wars as they have added to uncertainty. This research explores how the trade war between the US and China, indicated by an increase in tariffs, has affected India's financial markets, sector performance, export capability and foreign investment inflows. Descriptive statistics and regression techniques, using a sample from a survey of 99 respondents, have been used to look at the following four areas: (i) the impact of tariffs on foreign direct investment (FDI) and exports (ii) the impact of GSP benefits being removed due to the US ending these GSP benefits to India (iii) the effect of fluctuations in crude oil prices on various sectors and (iv) the position of India's MFN tariff rate as compared to the rates in other countries. The results of this investigation have produced inconsistent findings. The introduction of reactive tariffs does not appear to significantly change the performance of any industry but the rising price of crude oil is negatively and significantly correlated with performance in sensitive sectors. Descriptive analysis has indicated that the removal of Indian GSP rights and the changes to MFN tariffs have created moderate challenges to India's trade resilience and caused volatility in its merchandise export markets. Through this investigation, we provide an overview of the challenges faced by Indian policymakers and offer suggestions for improving the resilience of India against these challenges and enhancing India's position on the global market.

KEYWORDS: *Trade Conflict, Indian Capital Markets, Duty Modifications, Generalized System of Preferences Elimination, Oil Prices, Most Favored Nation Tariffs, Foreign Direct Investment, Export Competitiveness.*

INTRODUCTION
Over the past decade, trade wars have been a leading cause of economic disruption at almost every level across the globe. In 2018, the US-China trade conflict created major impacts on the developing economies such as India, which was also impacted by the instability of global supply chains. As a result of these trade wars, India has been affected in several ways, including changed levels of Foreign Direct Investment (FDI) flowing into India, a decrease in the export performance of its exports, reactions in sectoral-stock markets, and adjustment of tariffs imposed within India. Additionally, uncertainty created by the US's ending of Generalized System of Preferences (GSP) was also a cause of concern. Due to India's increased presence on the international stage and heavy reliance on imported energy sources, specifically crude oil, it is important to understand how global trade conflicts will affect India's domestic financial markets. This research will examine the relationships between these events to offer data-driven guidance for policymakers and industry stakeholders.

REVIEW OF LITERATURE
• **Yadav, A. (2025): The US-China Trade War,** Economic Policy Uncertainty (EPU), and Its Role in Return in the [Financial Markets of India] This paper investigates the impact of the US-China Trade War and Economic Policy Uncertainty (EPU) on India's Financial Market by employing an event study methodology to assess Stock Market Responses to Major Tariff Announcements. The research indicates that Stock Market Indices for India were significantly impacted in the short term following Trade Conflict Announcement Events, which suggests that Global

Trade Disputes have an impact on Local Equity Markets. This paper also emphasises how Emerging Markets, such as India, are susceptible to geopolitical turmoil and instability.

• **Wu, C. C. (2025):** This study focuses on the extreme risk spillover between major global equity markets. As a result of the US-China trade conflict, there was an increase in extreme risk spillover between equity markets, particularly to emerging markets. India's extreme risk has increased by virtue of changes in global risk perception. These results demonstrate the systemic impact of global trade conflicts on the overall marketplace.

• **Hoque, M. E. (2023)** The Impact of Inconsistencies In Global Trade Policies on Equity Exchanges throughout the World. Hoque studied the impact that trade policy uncertainty has had on equity exchanges throughout the world through the lens of trade policy uncertainty arising from the U.S., China, and Japan. The findings from hoque's study clearly substantiate the belief that uncertainty stemming from trade policy has had a significant border-to-border effect on the volatility of the Indian equity exchange during the trade war, as evidenced by large spikes in volatility during the trade war period in India. Hoque employed sophisticated econometric techniques to quantify spillover effects; this reinforces the idea that the international trade sentiment influences the equity exchange of India.

• **Che, Y. (2025) Pain or Gain: Trade War, Trade Deficit, and Tariffs** Che conducts research that investigates tariff avoidance tactics and the shifting of trade routes during times of international trade conflict. The results indicate that geopolitical change in the routing of Nigeria's exports impacts India's export companies by changing how the investor views the country as an exporting nation. This research demonstrates that trade wars affect financial markets in ways that are not directly related to efforts to avoid tariffs.

• **Reuters (April 7, 2025):** This news article discusses the impact that tariffs on the import and export of goods have had on the value of the Indian rupee versus the US dollar over the last three months. The drop in value was severe enough that it has caused a large loss in value for domestic stocks traded on the Indian stock exchange. As shown within the article, market responses were immediate, stating that international trade conflicts and the resulting global economic turmoil would continue to have detrimental effects across multiple sectors of the global economy and therefore the Indian economy.

• **Union Bank of India (2025 report): Stalemate in US-India Trade Negotiations:** This is a report that will assess the impact of the impasse on US-India trade negotiations upon Indian financial markets and to identify the potential adverse impacts of tariffs on Agricultural, Textile and Pharmaceutical sectors. It shows that investor confidence has been negatively impacted and that uncertainty has affected the macro-economic indicators and investor confidence. This provides a perspective that will be useful in formulating a policy regarding the assessment of financial markets.

• **Vlasova, E. (2022): Volatility Spillover between the Russia-India-China Triad.** In this research study, we examine how volatility is spreading between Russia, India, and China at the time of heightened global political risk, including the recent trade conflict. Our findings indicate that India has been increasingly experiencing a rise in volatility transfer associated with volatility changes occurring in both Russia and China and with rising levels of uncertainty throughout the world regarding trade. This paper looks at India's level of susceptibility to worldwide volatility transfers as part of its connection to larger regional issues and therefore supports the hypothesis that disturbances within the markets are interconnected in multiple ways.

• **Agarwal, A. (2024): Interconnectedness and Spillover Effects among Stock Markets**. According to Agarwal, global events, such as the trade war between the USA and China, have increased connectivity among stock exchanges across countries. As a result of this globalisation of stock exchanges, the financial relationship between India and other international markets has intensified and become stronger; however, at the same time, Indian stock markets have become increasingly susceptible to adverse economic fluctuations resulting from the trade war. The results of this study demonstrate how global economic sentiment impacts Indian investor behaviour.

• **The Reasonableness of Assumptions in Theoretical Models – Abrego, Riezman & Whalley (2006).** This study analyzes the negotiations conducted as part of the Tokyo Round. The authors evaluate whether the assumptions incorporated into models of trade are a realistic representation of actual trading behaviors by employing computational techniques. The findings provide insights into ways that trade patterns are likely to change if agents engage in

retaliation using non-tariff barriers. This work will assist in developing a better understanding of how well current models of trade conflict represent the realities of global trade.

• **Game Theory in Multilateral Trade Negotiations – Baldwin & Clarke (1987).** This article employs Computational Game Theory and Numerical Game Theory in studying Multilateral Trade Negotiations (MTN) throughout the Tokyo Round, focusing specifically on the influence of retaliatory Non-Tariff Barriers (NTBs) on trade disputes and revealing the methods through which governments behave strategically in international trade negotiations.

• **Algorithms for Identifying Equilibria in Repeated Games – Cronshaw (1997)**. In the study undertaken by Cronshaw, trade disputes are presented as continual games because individual countries are engaged in a multi-stage process to resolve trade disputes. By developing algorithms, the study attempts to determine equilibrium solutions as the outcome of an ongoing strategic interaction. This informs us on how trade disputes continue and become stabilised over time through repeated decisions.

• **Tariff Measures and Defensive Strategies – Deardorff & Stern (1987).** An analytical study presented by this paper demonstrate that nations utilise defensive tariff strategies when confronted with trade issues. Additionally, through the analysis, the authors provide insight into how the concept of "optimal tariff" has been applied by nations in relation to their reactions to trade disputes and thus are able to determine the best course of action to protect their domestic industries when reacting to international trade policy actions taken against them.

• **The World Trading System Economics – Bagwell & Staiger (2002).** This article analyzes a trade conflict model in which nations set tariffs that are politically optimal instead of socially optimal tariffs. These politically optimal tariffs are frequently dissimilar to the multilateral tariffs stipulated by international treaties. The study documents the political motivations associated with the implementation of protectionist trading policies.

• **Trade Wars versus Trade Discussions – Grossman & Helpman (1995).** The authors of this paper present evidence indicating that, when formulating trade policy, if governments were only focused on maximising social welfare, they would be more likely to establish politically optimal tariffs for their respective industries. In the example given in the paper, the authors illustrate how interest groups and political influences play a significant role in determining political optimal tariff levels and ultimately lead to trade wars or extended trade negotiations.

• **Potential Economic Effects of Global Trade Conflicts – Bekkers & Teh (2019).** Utilizing the WTO Global Trade Model, this research assesses the economic impacts of a global trade war over the medium term. It demonstrates that Very High trade conflicts can inflict dramatic losses in both economic activity and trade volume and significant reductions to global income. The research highlights the scale of macroeconomic impacts that could result from protectionist policies.

• **War and the World Economy – Schneider & Troeger (2006)**. The research looks at what happens to stock markets when there is a war or when there are international conflicts. In most cases, because of increased levels of uncertainty and risk associated with these conflicts or wars, markets tend to drop, but the authors also state that if the war or conflict leads to less uncertainty for the market, there may be times when the market's response is positive.

•**Armed Conflicts and Capital Markets, Kollias, Papadamou & Stagiannis (2010)** This study has shown how wars and international conflicts affect the financial markets. While generally speaking, the financial markets (as measured by stock prices) will fall due to increased levels of uncertainty and risk associated with wars and conflicts, the authors also note that in certain instances, if the war or conflict results in decreased uncertainty for a financial market, there may be instances in which the market reacts positively.

• **Diversifying Away the Risk of War, Omar, Wisniewski & Nolte (2017)** The authors of this study explore 64 international conflict-related occurrences. These events serve as a basis for their investigation into how these conflicts affect international stock prices. Based on the authors' findings, they conclude that when there is military activity or political instability within a country, investors in that country and abroad will experience significant abnormal negative returns on their investments. These findings suggest that geopolitical conflict creates economic risks for the global marketplace.

• **Economic Costs of the Russia–Ukraine War, Liadze et al. (2023)** The authors employed the NiGEM modeling system to assess the economic impact of the Russia-Ukraine conflict. The authors noted that there would be significant longer-term negative consequences to the economy as well as increases in costs to purchase energy, increases in inflation, and declines in international trade as a result of the ongoing conflict. Their analysis also includes future estimates of economic loss as a result of the conflict.

• **Hollowing-Out of India's Manufacturing Sector, Banga (2014)** The findings from the study highlight a reduction in the proportion of Indian manufactured goods exported, alongside an increase in reliance on imported goods. The author of the report believes that these trends are indicative of the "hollowing-out" of India's domestic manufacturing industry and has proposed that India must expand its presence in global supply chains so as to maximise value-creating activities and establish itself as a competitive player in the global market.

STATEMENT OF THE PROBLEM

The ongoing global trade disputes (specifically between the United States and China) have produced a high degree of uncertainty throughout both international trade and the financial markets. As an emerging market economy with an extensive reliance on globalized supply chains for many products — most notably crude oil — India stands out as being particularly at risk from such disruptions/chaos in the marketplace. India has experienced reductions in investor confidence, capital flight, and volatility due to increased tariffs/retaliatory tariffs that have come about as a result of the current trade conflict. In addition, India's removal from the US Generalized System of Preferences (GSP) has raised concerns regarding the competitiveness of certain key Indian export industries.

The response of India to this situation has included a series of changes in terms of tariffs on specific products related to protectionist initiatives, including 'Make In India' that have resulted in many discussions in regard to how these new tariff regimes will ultimately influence foreign direct investment (FDI) as well as export performance. While the change in these regimes is very important, there continues to be a lack of empirical research that examines how these policies impact the financial markets of India holistically. Most of the available research continues to focus on broader issues, rather than examining the effects of these policies on the specific impacts on India. This creates a significant gap in the general understanding of how external disruptions and domestic changes to policy affect the sectoral performance of stocks, trade activities, and ultimately economic resilience of India. Therefore, the overall aim of this study is to assess the simultaneous mutually exclusive effects of both the events related to global trade tensions, as well as the events related to changes in government policy on the financial markets of India in particular.

RESEARCH GAP

1. There is a need for empirical research exploring the combined overall and sectoral effects of domestic initiatives, such as India's Make in India program, and the ongoing global trade conflict. This topic has not been sufficiently addressed in previous studies.
2. There is a lack of analysis on the specific impacts of the global trade conflict on India and its sectors, as existing research often focuses on the broader Asia-Pacific region.
3. Specific subsidy effects under domestic policies like Make in India, including capital subsidies, interest equalization programs, investment allowances, and duty drawback schemes, are often left out of models analyzing trade wars.
4. There is a need for econometric evaluation to determine the influence of tariff changes on key economic indicators like industry productivity, foreign direct investment (FDI), and export competitiveness.
5. Research is needed to assess how strategies such as regional trade agreements, digital trade, and supply chain resilience can effectively reduce risks associated with geopolitical tensions and trade disputes.

OBJECTIVES OF THE STUDY

1. Measure how changes to tariffs affect India's foreign direct investment (FDI) and the competitiveness of its exports.
2. Examine the patterns and changes in India's GSP-covered exports to the United States before and after its removal.
3. Investigate the relationship between fluctuations in global crude oil prices and the stock market performance of key Indian sectors that are vulnerable to imported materials.

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4. Evaluate the historical trends of India's Most-Favored-Nation (MFN) average tariff rates compared to major trading partners to define India's protective trade measures.

HYPOTHESES OF THE STUDY

Objective 1: Effect of Reactive Tariffs on FDI & Exports

• H_{01}: Changes to reactive tariffs do not significantly impact India's FDI or export competitiveness.
• H_{11}: Changes to reactive tariffs significantly affect India's FDI or export competitiveness.

Objective 2: Impact of GSP Abolition

• H_{02}: The removal of India's GSP status has not significantly reduced GSP-covered exports to the United States.
• H_{12}: The removal of India's GSP status has significantly lowered GSP-covered exports to the United States.

Objective 3: Crude Oil Prices & Sectoral Stock Returns

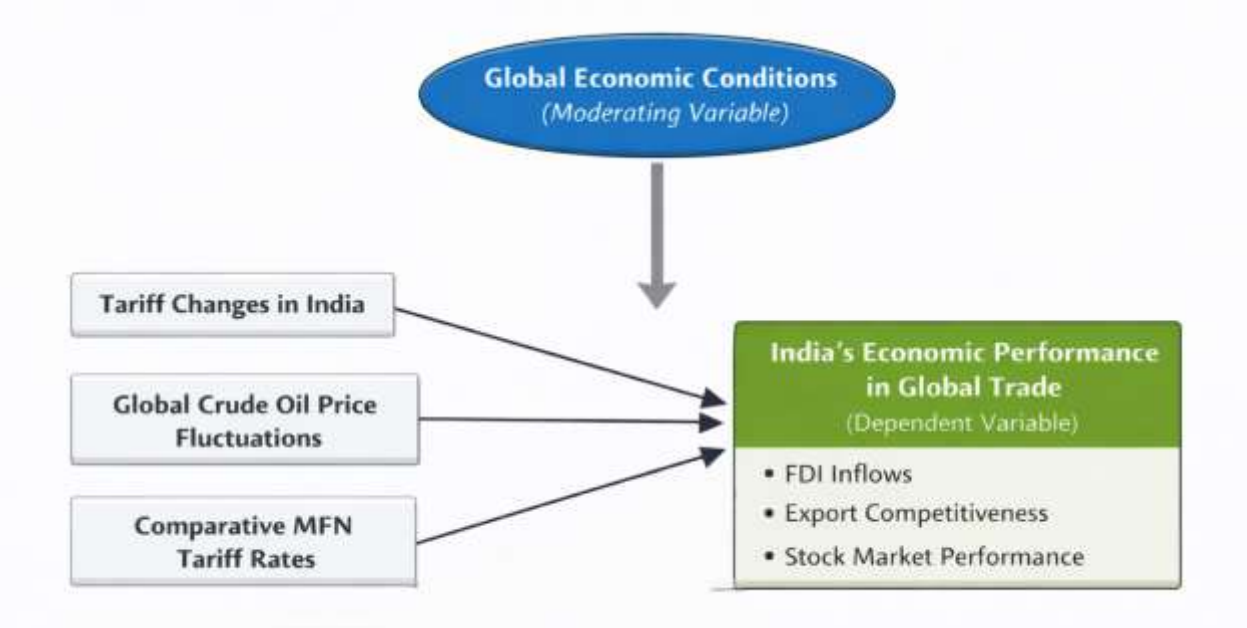
• H_{03}: Changes in crude oil prices do not significantly correlate with the stock returns of Indian sectors affected by oil prices.
• H_{13}: Rising crude oil prices have a significant and negative effect on the stock returns of Indian sectors sensitive to oil.

Objective 4: MFN Tariff Comparison

• H_{04}: India's MFN tariff rate is not meaningfully higher than that of its major trading partners.
• H_{14}: India's MFN tariff rate is significantly higher than that of its major trading partners.

CONCEPTUAL MODEL

Trade Conflict Factors → Tariffs → FDI/Exports → Market Responses
Oil Price Instability → Sectoral Stock Returns
MFN Tariffs → Competitiveness



DATA ANALYSIS & INTERPRETATION

Objective 1: Regression Analysis

We analyzed the basic relationship between Industry Sector as a dependent variable and Quantitative Impact Rating as an independent variable using linear regression. We used a sample size of 99 for this analysis. The analysis found that Quantitative Impact Rating and Industry Sector were not statistically related to each other. Additionally, the degree of correlation (r = 0.076) was very low, with a weak positive correlation. However, the relationship did not

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reach any level of statistical significance (p = 0.227 on a one-tailed basis). Additionally, the regression analysis only accounted for 0.6% of the total variation in Industry Sector ($R^2 = 0.006$) and therefore indicated very little explanatory power. The overall regression model for this analysis was also not statistically significant (F = 0.566; p = 0.453). Although the regression coefficient for Quantitative Impact Rating was positive (B = 0.389), it did not achieve statistical significance and also had a t-value of 0.753 (p = 0.453) and a 95% CI that included zero. The conclusion of this study is that the variable Quantitative Impact Rating does not have a strong predictive ability with regards to determining which Industry Sector an individual is classified as being employed in; therefore, the null hypothesis was accepted.

Regression Results Table

Statistic	Value
Dependent Variable	Industry Sector
Independent Variable	*Quantitative Impact Rating*
Sample Size (N)	99
R	0.076
R^2	0.006
Adjusted R^2	−0.004
F value	0.566
Sig. (p)	0.453
B (qir)	0.389
t value	0.753
Sig. (p)	0.453
Result	Not Significant

Objective 2: Interpretation of Descriptive Statistics (Impact of GSP Abolition)

For the descriptive statistics for each of the five statements regarding the impact of the abolition of GSP preferences on businesses within the US, there were a total of 99 valid responses for each statement. The median range of the GSP responses was between 2.29 and 2.54. The overall mean across all statements indicates that the response pattern fell between the range of "agree" (2) and "neutral" (3); that is, respondents tended to be undecided but closer to agreeing with the response options related to this area of the business environment. The highest median response value (2.54) relates to the statement regarding the effect of an increase in the type and/or number of items available for sale and/or the ability of firms to sell more products in their respective market or markets today as an effect of the GSP abolition. This implies that most firms responding agree that this type of adjustment is now a part of their post-GSP business model. In contrast, the lowest median response value (2.29) relates to the statement regarding a decline in price competitiveness as a result of GSP abolition; therefore, there is a lower level of agreement surrounding this statement when compared with the others. Standard deviations across all statements were between 0.56 and 0.59. Uniform responses and limited variability indicate that respondents exhibited similar responses to the statements regarding the GSP abolition. This finding also supports the conclusion that response distributions were symmetric because the mean and median values were very similar for all statements. Stock data show that the most common responses fell either between "agree" (2) and "neutral" (3); therefore, a wide range of agreement exists for each of the GSP statements. All variables exhibit a negative skew, which means that there were more respondents who agreed with the statements. The negative kurtosis values across the properties indicate that uniformity exists in the distributions without any extreme clustering around the central point. Overall, the descriptive statistics suggest that participants recognize the negative effect of a GSP abolition and that significantly more firms will experience an increase in costs, or market changes and experiences other forms of negative consequences, as after the GSP abolition occurs.while a considerable portion remains neutral.

Objective 3: Regression Analysis

The dependent variable in the regression analysis was the Industry Sector, while the independent variable examined was the Regression Between Groups (N=99). The results indicate a statistically significant negative correlation between the Regression Between Groups and the Industry Sector. This correlation is weak but should be regarded as statistically significant. (r = -0.217, p = 0.016, one-tailed) The amount of variance explained by the regression model for the Industry Sector is 4.7% (R^2=0.047). Overall, the regression model is statistically significant (F=4.771, p=0.031) and the Regression Between Groups regression coefficient is negative and statistically significant (B=-1.075, t=-2.184, p=0.031) with its 95% confidence interval not including 0. Therefore, an increase in the Regression Between Groups

leads to a decrease in the Industry Sector value. Consequently, the Regression Between Groups variable is a significant predictor of the Industry Sector variable, and thus the null hypothesis is rejected.

Regression Results Table

Statistic	Value
Dependent Variable	Industry Sector
Independent Variable	Regression Between Groups
Sample Size (N)	99
R	0.217
R^2	0.047
Adjusted R^2	0.037
F value	4.771
Sig. (p)	0.031
B (rbg)	−1.075
t value	−2.184
Sig. (p)	0.031
Relationship	Negative, Significant

Objective 4: Evaluation of Descriptive Statistics (MFN Tariff Trends)
Data from 99 respondents produce descriptive statistics regarding India's MFN tariff trends associated with each of the five statements provided.

The mean of all values shows an average score on a scale, from 2.42 to 2.55, which indicates that respondents tended to indicate agreement to a neutral or neutral position, the latter being slightly tilted in the direction of agreement. The majority of respondents had an average value of 2.55 regarding their belief that MFN Tariff increases lead to more domestic sourcing while the second-highest average value of 2.53 indicates that tariff differences negatively impact the competitiveness of a country's exports. Both of these values strongly indicate agreement regarding the impact of MFN tariffs.

The statement regarding how MFN tariff changes affect import prices received the lowest average value of 2.42 (but the average score indicates mild agreement).

Across all five statements, the standard deviation is relatively low. Thus, there are not significant differences in responses across these 99 firms. Also, each statement's median reflects the same pattern as its average score, indicating relatively stable central tendencies.

For most statements, the majority of responses indicate "agree" (3). However, for the statement regarding how MFN Tariff increases affect import prices, "agree" (2) was more common than "agree".

All five statements indicate negative skewness since there were more respondents answering in the agreement direction for these statements than in the neutral direction. Each statement has negative kurtosis (distribution shape), indicating a flat distribution of responses with little to no clustering of responses.

Most of the people surveyed had either an agreement or neutral view regarding import cost, sourcing from within the country and indications of protectionist policies shown through the frequency distribution. The amount of people surveyed having an agreement (in each case) was greater than the number of people surveyed responding as being neutral toward their perception of import cost.

In conclusion, these results would suggest that firms consistently hold a moderate to strong belief that MFN tariffs influence a firm's conduct, firm's sourcing tactics and competitiveness. Therefore, the authors would conclude that India's current trade policy is more of a moderate protectionist trend rather than being a significant protectionist trade policy..

FINDINGS

- Policies such as Make in India generated reactive tariffs that did not display a statistically significant impact on general industry performance or industry-wide production capabilities.
- The limited (or no) impact that these policies had on foreign direct investment (FDI) and export performance may indicate that companies did not respond to these changes in a way that increased their competitiveness for exports or the level of FDI they were receiving.
- Descriptive evidence indicates that removal of the Generalized System of Preferences (GSP) caused little impact on companies; instead, removal was primarily characterized by increased production and export costs.
- The GSP withdrawal caused companies to change product mix and adjust product prices and marketing strategies.
- Regression analysis indicates that crude oil prices are negatively correlated with stock returns for companies in various sectors. Increased crude oil prices significantly decrease stock performance, and the relationship is stronger for sectors dependent upon oil, such as utilities and transportation.

CONCLUSION

Although retaliatory tariffs have had no direct influence on FDI or export competitiveness, the elimination of GSP has had a moderate impact on exporters. Oil prices were the most significant influence on the performance of Indian sectors; therefore, Indian industry still relies on imported energy for its production processes. The MFN tariffs are beginning to reflect a trend of moderate protectionism through trade policy. Together, these factors illustrate both external and domestic influences on financial stability in India. Policymakers must develop a balanced trade policy that supports Indian producers and minimizes their exposure to potential external shocks.

LIMITATIONS OF THE STUDY

• This study was based on a convenience sample of 99 individuals in India, which has limited influence in regard to representing an entire industry impacted by international trade disputes.
• The research relied on convenience sampling and thus limited the ability to apply the study to the entire population.
• The cross-sectional design allowed for an analysis of perceptions from only one time point in time and does not account for any changing perceptions over time.
• All data collected were based on self-reported information, which could potentially contain bias, particularly for respondents answering complex economic questions.
• The results of this study used measures of perception as compared to using any or all available secondary quantitative data.
• Due to lack of available data, the study did not provide an in-depth investigation into the differences between sectors of Indian financial markets.

FUTURE SCOPE OF THE STUDY

Longitudinal or time-series analysis to follow the changes in FDI, exports, and the markets related to trade conflicts over time would allow for longer-term studies of the effects of trade disputes. Industry-level studies will provide a more detailed understanding of how distinct industries (eg. textiles, automobiles, pharmaceuticals) have experienced tariff changes or global disruptions. Comparative research between India and similar countries will provide a clearer picture of each country's relative competitive advantage; use of advanced econometric models will clarify the causal relations between tariffs, oil prices and policy changes. Digital trade, supply chain resilience and regional trade agreements may mitigate the risk of global trade tensions, and future studies should focus on these topics.

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