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Trade war may be put on hold?

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The Chinese government confirmed yesterday that it has received an invitation from the US government for another round of trade negotiations. We take this as a positive development. The two sides will likely hold the meeting soon. We doubt they will reach a deal to resolve the trade dispute completely in this round, but the tariff on the US$ 200bn Chinese exports will likely be put on hold until the negotiation is over. We also think it is possible that the tariff will be put on hold further, depending on the outcome of the talks, to avoid hurting US consumers ahead of the midterm elections.

We recently highlighted the potential damage of the 25% tariff on the US$ 200bn exports (see our report here). There are $78bn of consumer goods in the $200bn list, compared to only $3.7bn in the $50bn list announced before. They include consumer goods such as furniture, vacuum cleaners, air conditioners, etc. We think the US side initiated the meeting, maybe because it is concerned that imposing such a tariff ahead of the midterm elections may be costly.

We believe China is happy to engage in the meeting and delay/avoid the tariff, but there is also a sense of doubt, given what happened in May. Vice Premier Liu He visited the US to negotiate in May and declared that the trade war was over after the talks, only to find the US side changed its position soon afterwards. The most likely outcome of the meeting is probably "the two sides had constructive discussions, and will report to their leaders respectively for further negotiations". The technocrats on both sides will likely work out a list of issues for the two Presidents to decide at the G20 meeting on Nov 30 – Dec 1.

Meanwhile, China's export growth has not been affected much by the threat of a trade war. The main damage to the Chinese economy is through the financial market channel – the weak stock market likely leads to a negative wealth effect, which hurts consumption. China will likely keep the current policy stance: with interest rates stable at low levels, more local government spending through bond financing, but refrain from large-scale stimulus.

Appendix 1

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