

Trade Bullets: Interim Deal on Life Support

In [Osaka Deal Do-Over?](#) (9/11/19) I outlined a possible “Ag for Android” limited “cease-fire” deal that was taking shape, and opined that “if the Chinese offered it, Trump should jump at it.”

He does not appear to be jumping...

- Friday’s **cancellation of the Chinese delegation’s trip to U.S. farm country is a negative data point** regarding a possible “interim deal.” The U.S. side pulled the plug because they didn’t want the Chinese riling up farmers by dangling massive Ag orders *that are likely never to arrive*.
- In announcing the trip before clearing it with negotiating principals on the U.S. side, **the Chinese again illustrated their capacity for miscalculation** of U.S. political dynamics and sensitivities.
- China’s provision of tariff waivers for the purchase of 2-3m tons of beans (for reference, the U.S. sold 21.4m tons to China in 2017) signals they are serious about Ag purchases, but offering little else of substance.
- [Signals from China](#) continue to indicate **they are bringing no new flexibility on established red lines** to this negotiating round
- It’s likely that **China’s strategy is nothing more than to buy some peace and quiet** on the trade flank to get through the big political events ahead in October
- President **Trump is** surprisingly, and I think genuinely, **cool to a “limited” deal**
- **The rhetorical barrage Trump delivered at the UN on Tuesday was unusual.** The verbal hit jobs have generally been delivered by Pompeo, Pence and others, allowing Trump to play the role of “good cop” and BFF to President Xi. Not anymore:

“Not only has China declined to adopt promised reforms, it has embraced an economic model dependent on massive market barriers, heavy state subsidies, currency manipulation, product dumping, forced technology transfers and the theft of intellectual property and also trade secrets on a grand scale. As far as America is concerned, those days are over.”

“The American people are absolutely committed to restoring balance in our relationship with China. Hopefully, we can reach an agreement that will be beneficial for both countries,” Trump said. “As I have made very clear, I will not accept a bad deal.”

- Trump also drew a clear red line on Hong Kong:

*“The world fully expects that the Chinese government will honor its binding treaty made with the British and registered with the United Nations, in which China commits to protect Hong Kong’s freedom, legal system and democratic ways of life. **How China chooses to handle the situation will***

say a great deal about its role in the world in the future. We are all counting on President Xi as a great leader.”

- **Protestors in Hong Kong should be emboldened** in the belief that China will face significant geopolitical consequences if it overtly intervenes to quell the crisis.
- **President Trump can't possibly do a deal of any substance while China is potentially poised to roll into Hong Kong.**
- Though it garnered less attention, the [U.S. organized a sideline event involving 30 countries](#) which condemned China's "horrific campaign of repression" in Xinjiang. That **may prove even more provocative to the Chinese** than Trump's speech.
- The impeachment kerfuffle is inauspicious for the trade talks. **Nancy Pelosi may have unwittingly set herself up as a fall guy** for the failure of trade talks that Trump doesn't seem to have much interest in anyway: "how am I supposed to get a great trade deal done with this witch hunt going on?"
- At this point both sides seem to be going through the motions. **Trade remains an event-risk overhang to risk asset markets** – one of many that loom in October:
 - Oct 1 counter-demonstrations in Hong Kong
 - Rising risk of Chinese intrusion into HK after the Fourth Plenum mid-month
 - Brexit
 - The [likely imposition of aggressive Airbus-related tariffs](#) on Europe
- Expect markets to remain headline-driven. **Prospective returns are not normally distributed.**
- Markets still need to come to grips with "**China decoupling.**" I'm strongly of the view that such a reality is **a more digestible outcome for global risk assets than is generally perceived so long as it doesn't throw China into imminent crisis.**
- The Hong Kong protests have emerged as a complicating factor which significantly increases the risk of the China crisis tail.