Economic Commentary

QNB Economics
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Face saving US-China trade deal is just political smoke and mirrors

Introduction: Last week, President Donald Trump announced a "substantial phase one" trade deal with China via his Twitter account @realDonaldTrump. He highlighted that it was "by far, the greatest and biggest deal ever made for our Great Patriot Farmers". However, agriculture is just one of a number of areas of tension between the US and China relating to trade.

> **Donald J. Trump** @realDonaldTrump Follow
>
> The deal I just made with China is, by far, the greatest and biggest deal ever made for our Great Patriot Farmers in the history of our Country. In fact, there is a question as to whether or not this much product can be produced? Our farmers will figure it out. Thank you China!
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> 7:09 AM - 12 Oct 2019

Here we outline some of the details of the so-called "deal" in the context of the memorandums of understanding between the countries developed by trade experts in March: agriculture, currency, forced technology transfer and cybertheft, intellectual-property rights and non-tariff barriers to trade (see Progress not perfection in US China trade talks). Finally, we conclude with our view about what it means for the the global economy with reference to the International Monetary Fund's (IMF) October update of its World Economic Outlook (WEO).

Details of the "deal": The US and China appear to have agreed on the outlines of a partial trade agreement. Trump hopes the final deal can be signed by himself and Chinese President Xi Jinping at the Asia-Pacific Economic Cooperation meetings in Santiago, Chile in late November.

The key step forward appears to be a commitment from China to significantly increase purchases of US agricultural commodities. Reports suggest that progress was also made in other areas including intellectual-property, financial services and currency, but details remain vague. However, the most difficult issues to resolve remain outstanding including US complaints about intellectual-property theft, forced technology transfer and Chinese industrial subsidies.

In return, the US has delayed tariff increases from 25% to 30% on USD 250 billion of Chinese imports that were scheduled for October.

However, we need to point out that it's not yet a done deal. The devil was in the detail when discussions on a previous agreement fell apart in May. Indeed, even Trump concedes that the substance is yet to be written and that it would be just the first phase of what he hopes will become a broader agreement.

Further tariffs are still due to be implemented on another USD 160 billion of Chinese imports in December. The US began by focusing tariffs on intermediate goods so that additional costs would hit firms profits and supply chains before consumers. However, this further round of tariffs will inevitably include more consumer products increasing the amount of harm the US is inflicting on itself.

Conclusion: Refering back to the view we expressed two weeks ago, we see the US and China as long-term strategic rivals. Hence, we believe that the current cease-fire will be short-lived and may not last beyond the 2020 presidential election. Indeed, in the longer term, we consider further escalation to be more likely than de-escalation (see US-China trade war a significant headwind for global GDP growth).

As we anticipated the IMF has substantially downgraded its forecast for global GDP growth in its October WEO. The IMF describes the global economy as being in a "synchronised slowdown" and has downgraded its forecast for global GDP growth to only 3% in 2019, the slowest since the global financial crisis. The IMF then forecast a modest recovery to 3.4% in 2020, but this was also revised lower relative to April WEO.

Notably, the IMF has explicitly estimated the impact of the US-China trade war as causing a reduction of 0.8% in the level of global GDP by 2020.

As can be seen from our writing on the Fed and the ECB, we also share the IMF's view that monetary policy has played a significant role in supporting the global economy. The IMF estimates that without monetary support from central banks global growth would be 0.5 percentage points lower in both 2019 and 2020.

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