

Greater China

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Trade deal: is this time different?

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- China's compromise not to insist on the removal of existing tariff as pre-condition for a trade deal is encouraging.
- The documentation of phase one deal in black and white in the next one month will be the first testing point.
- The road to a complete deal will depend on the negotiations on intellectual property and technology transfer.
- Five hot topics including the planned tariff hike on 15 Dec, Huawei, US entity list, currency manipulation designation and existing tariff are not addressed in this agreement. Those could be the sources of uncertainty in future.
- This time may be different as timing could be the catalyst for both sides to go ahead with the talk without derailing the situation.

Although the news flow prior to the trade talk is mixed after the US added more Chinese companies into the entity list, a phase one trade deal has been reached on 14 Oct, which will delay the additional tariff hike previously scheduled on 15 Oct. Five areas have been covered in phase one including agriculture purchase, opening of China's financial services, currency agreement, intellectual property and technology transfer. The first three areas have been covered entirely in phase one while the latter two will be discussed further in phase two.

As mentioned by President Trump that the US is surprised by China's generous offer to increase its purchase of US agriculture products to US\$40-50 billion per annum from currently US\$8 billion, much higher than US's previous target of about US\$20 billion. Put quantity of agriculture purchase aside, we think China did make compromise to reach this partial deal as removal of existing tariff is no longer the pre-condition for a bilateral deal.

Table 1: A revisit of China's three red lines

China's previous red lines	Current update after phase one
1) China demands the US to remove entire existing tariffs	China no longer insisted on the removal of existing trade deal
2) The US should comply with the previous target for agriculture product purchase instead of keeping increase the target	According to President Trump, China offered more than what the US expected in terms of agriculture purchase.
3) The wording of the text in the agreement should be equitable	<i>Pending.</i> Market will watch how is the phase one deal papered in black and white in the next one month. No news on US forcing China to change its law.

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What's next?

Market will watch out for two things going forwards. **First**, the documentation of the phase one deal is expected to take about one month. Ideally, the deal will be signed formally during the APEC meeting in Chile in mid-November. Second, the phase two will also start very soon. As mentioned by the President Trump, three areas including agriculture, financial services and currency have been covered by phase one entirely. As such, phase two will mainly cover intellectual property and technology transfer with key focus will be on technology transfer. President Trump did not rule out the possibility of phase three to cover technology transfer. Overall, we think it remains uncertain how far we are from the complete trade deal.

Table 2: Road to a complete trade deal			
Areas	Phase one	Phase two	Phase three?
Agriculture purchase	Entirely covered		
Financial Services	Entirely covered		
Currency	Entirely covered		
Intellectual property	A large part covered	The remaining part	
Technology transfer	Some covered	Largely done	May be extended

Five uncertainties remain

Although the 15 Oct planned tariff hike has been officially delayed, there are at least five hot topics not being addressed in the phase one talk.

Table 3: Five Hot topics not addressed in Phase one	
The second tariff hike on 15 Dec	Subject to President's final decision
Huawei	A separate process and is not part of agreement
The expanding entity list	Will look at the list and a separate determination will be made on which companies on the list
Currency manipulation	A decision will be made by US Treasury
Existing tariff	No update: but Trump said he likes tariff

Is this time different?

The positive headline is encouraging. However, we saw the same movie before in April. President Trump thought this time is different as both negotiators have known each other a lot better after a few rounds of back and forth. We think timing could be the catalyst for both sides to go ahead with the talk without derailing the situation as the US is approaching the new Presidential election.

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