Market Note

3 December 2018

China and the US agree to halt new tariffs for 90 days

On 1 December (Argentina Time), China and the US agreed to a ceasefire to keep their trade war from escalating with a promise to halt the imposition of new tariffs for 90 days after high-stakes talks in Argentina between US President Donald Trump and Chinese President Xi Jinping, including no escalated tariffs on 1 January 2019[1].

In this market note, Ronald Chan, Chief Investment Officer, Equities, Asia (Ex-Japan), believes the markets have probably seen the peak of trade frictions between the two countries. Markets and sectors that have been most impacted should react positively to the outcome in the near-term, in particular, China A-shares, North Asian bourses, and exporters.

Pause tariffs hike on 1 January 2019

At the working dinner after the conclusion of the 13th Group of 20 Summit, President Xi and Trump had an in-depth exchange of views on Sino-US relations and agreed not to impose new tariffs.

On trade, President Trump has agreed that on 1 January 2019 he will leave the tariffs on US$200 billion of Chinese imports at the 10% rate, and not raise it to 25% at this time. China will agree to purchase a not yet agreed upon, but very substantial amount of US agricultural, energy, and industrial products. China has also agreed to start purchasing agricultural products from US farmers[2].

President Trump and President Xi have agreed to immediately begin negotiations on structural changes with respect to "forced" technology transfer, intellectual property protection, non-tariff barriers, cyber intrusions and cyber theft, and services and agriculture. Both parties agree that they will endeavour to have the negotiations completed within the next 90 days, and will revisit the tariff issues should the outcome from the negotiations not be satisfactory[2].

Market implications

According to Ronald Chan, Chief Investment Officer, Equities (Asia ex-Japan), the temporary ceasefire on trade tariffs between the US and China was as expected and should be seen as a positive outcome. Principle agreements reached between the two leaders will provide the framework for details to be worked out in the next three months, especially on intellectual property and non-tariff barriers. According to Chan, numerous factors contributed to this agreement: pressures have been accumulating on both sides, including China's slowing macro data, as well as announced auto plant closures in the US and rising cost concerns from US corporates.

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[1] Reuters, Bloomberg, 2 December 2018.
[2] White House, 2 December 2018.

Given the above and if the principle framework is maintained, Chan believes that the markets have probably seen the peak of trade frictions between the two countries. Moreover, investors' confidence in markets will be rebuilt. Markets and sectors that have been most impacted should respond positively to the outcome in the near term, in particular, China-A shares, North Asian bourses, and exporters.

Winson Fong, Senior Portfolio Manager, Greater China Equities, acknowledges that China and Hong Kong equities have been de-rated in 2018, amidst considerable market corrections triggered by the Sino-US trade dispute. While complete blockage of the Chinese technology sector by the US remains the greatest risk facing companies, particularly in the Greater Bay Area (GBA), Fong echoes that most potential risks have been priced in by the market. Fong believes that improving investor sentiment is a key premise for a market recovery, as equities will be re-rated once concerns over these risks dissipate, and when markets shift focus back to the fundamentals of the GBA companies.