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China and US agree to resume trade negotiations but issues remain

Chinese President Xi Jinping and US President Donald Trump met on 29 June on the sidelines of the G20 summit, and agreed to a trade war truce and resumption of bilateral trade talks. We will continue to closely monitor developments in this regard.

Xi and Trump agree to hold off on new tariffs and to resume trade talks

On 29 June, President Xi and Donald Trump held a highly anticipated meeting on the sidelines of the G20 summit in Osaka, Japan. The two leaders agreed to suspend any new tariffs against each other's products 'for the time being', and to resume trade negotiations.

Trump described the meeting as a 'very, very good meeting, better than expected'. On the issue of Huawei, Trump suggested that US companies could sell to the Chinese tech giant again as long as the products involved do not threaten US national security, but he is 'leaving Huawei towards the end [of trade negotiations]'. Trump also said that China agreed to buy a 'tremendous' amount of US goods to reduce the trade imbalance. Meanwhile, China's Foreign Ministry said in a statement that negotiators from both sides will discuss specific issues, without giving any details.

Our take

The result of talks between Xi and Trump is better than many people predicted ahead of the event, with the two leaders agreeing to another trade war truce, resumption of trade talks, and a possible relaxation of the US ban on Huawei.

However, the trade war truce suggests only a suspension of the escalation of the China-US trade conflicts, not a resolution of the trade war, as the 25% additional tariffs on US$250 billion of Chinese imports will stay in place while trade negotiations are in progress. These tariffs will continue to hit Chinese exporters and disrupt global supply chains in the near future.

Moreover, although the two leaders agreed to resume trade negotiations, the two sides are no nearer to reaching a comprehensive trade deal to end the trade war. Several major issues still need to be addressed in the trade talks, including: (1) China reportedly continues to resist concessions on some US demands on 'structural changes' in China's economic policy; (2) the US reportedly prefers to keep some of the additional tariffs as leverage even if the two countries reach an agreement; and (3) whether other US sanctions on China such as the export ban on Huawei could be removed. Given these difficult hurdles, we do not expect a smooth negotiation process. If the two countries fail to reach an agreement, the US could still impose 25% additional tariffs on US$300 billion of Chinese imports.

US domestic politics could also complicate the trade talks. While many people assume that Trump would like to reach a trade deal to boost his popularity before the US presidential election next year, it is equally possible that Trump finds a tough stance on China will draw him greater bipartisan support. If Trump's decision to de-escalate or re-escalate trade tensions with China becomes a political calculation, the already-difficult bilateral trade negotiations could be facing additional complications. Besides, another flip-flop by the US administration is not totally out of the question, given Trump's track record of stance-shifting.[1]

In the longer term, even if the two countries can reach a comprehensive trade agreement to end the trade war, broader uncertainties and tensions (such as the escalating technology war) between the two countries are likely to remain for a long time, as the key issue between China and the US is geopolitical rivalry instead of trade.

[1] On 5 May this year, just two days after Trump said that China and the US were 'getting close to a very historic, monumental deal', Trump announced that the US tariff rate on US$200 billion worth of Chinese goods would be raised from 10% to 25%. On 29 May 2018, the US government announced that it would impose 25% tariffs on US$50 billion worth of Chinese goods, tearing up an agreement reached only ten days ago by the two countries to put the tariffs 'on hold'.

Implications for our sourcing business: We need more diverse and flexible supply chains

The ongoing China-US trade war has caused disruptions in the global trade landscape, bringing fresh challenges and greater unpredictability to our sourcing business. Under such circumstances, production and supply chains now need to be even more diverse, agile, and technology-driven. Businesses with a strong global supplier network and deep relationships with suppliers will be in the best position to meet the new challenges. To navigate the challenging situation, businesses should continue to carry out strategic planning and re-planning for their supply chains, through diversifying sourcing base, nearshoring and onshoring production, and digitizing supply chains.

FUNG BUSINESS INTELLIGENCE

Fung Business Intelligence collects, analyses and interprets market data on global sourcing, supply chains, distribution, retail and technology.

Headquartered in Hong Kong, it leverages unique relationships and information networks to track and report on these issues with a particular focus on business trends and developments in China and other Asian countries. Fung Business Intelligence makes its data, impartial analysis and specialist knowledge available to businesses, scholars and governments around the world through regular research reports and business publications.

As the knowledge bank and think tank for the Fung Group, a Hong Kong-based multinational corporation, Fung Business Intelligence also provides expertise, advice and consultancy services to the Group and its business partners on issues related to doing business in China, ranging from market entry and company structure, to tax, licensing and other regulatory matters.

Fung Business Intelligence was established in the year 2000.

About Fung Group

Fung Holdings (1937) Limited, a privately-held business entity headquartered in Hong Kong, is the major shareholder of the Fung Group of companies, whose core businesses operate across the entire global supply chain for consumer goods including trading, logistics, distribution and retail. The Fung Group comprises 42,000 people working in more than 40 economies worldwide. We have a rich history and heritage in export trading and global supply chain management that dates back to 1906 and traces the story of how Hong Kong and the Pearl River Delta emerged as one of the world's foremost manufacturing and trading regions. We are focused on both creating the Supply Chain of the Future to help brands and retailers navigate the digital economy as well as creating new opportunities, product categories and market expansion for brands on a global scale.

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