

China Weekly Letter

A roller coaster week should end with interim deal

- An interim deal between US and China is still on the table despite US blacklisting of more Chinese companies. Trump announced he will meet the vice Premier on Friday, which bodes well for the result of trade talks.
- Another area of tension has opened up in the US-China confrontation with the suspension of NBA pre-season broadcast in China.
- Brace for another 'lowest growth in 30 years' headline when Q3 GDP is released next week. The headline can be made every year, though, as growth is slowing on a structural basis.

Trump to meet Chinese vice premier is a positive sign

It has truly been a bit of a roller coaster up to the US-China trade talks starting today in Washington. The latest news has been US President Donald Trump's *tweet* that he will meet China's top negotiator Liu He on Friday, which he has only done when talks have gone well. So this is fairly good news.

Earlier this week, though, US *blacklisted* another 8 Chinese companies including some of China's top AI companies and suppliers of surveillance equipment in the Xinjiang province. The US also imposed *visa restrictions* on Chinese officials linked to the detention of Muslims in the Chinese province. China strongly condemned the actions and warned of retaliation. Some sources say China plans tighter visa restrictions for US nationals with ties to anti-China groups. The Chinese foreign ministry spokesman said "*stay tuned*" when asked if China would retaliate to the US blacklisting of more companies. As if this wasn't enough, another story broke that the White House is considering a *limit on Chinese stocks* in US government funds. The range of negative news threw cold water on expectations for an interim deal.

However, on Wednesday China signalled that an interim deal was still on the table and *FT* reported that China would offer to buy 10 million tonnes of US soybeans in exchange for US taking tariff hikes off the table.

Today Bloomberg reported that the US looks to add a currency pact into the interim deal. Supposedly such a pact had been agreed to before the talks broke down and including it in an interim deal might remove one (of many) stones on the way to a broader deal eventually.

Comment: We stick to our view that there is a 60% probability of an interim trade deal. As a minimum, such a deal would include China buying agricultural goods and the US taking tariff hikes off the table again. As we've argued in past weeks, both sides would have an interest in that, see for example *US-China Trade – 60% probability of an interim deal*, 2 October 2019. The two sides will try to get other things into a deal but it remains to be seen if they can agree on this. The developments have shown again that China

Recent China Research

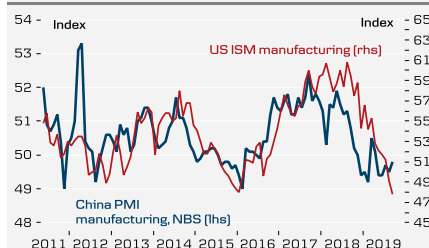
China Weekly Letter – Is the Chinese business cycle turning?, 4 October 2019

US-China Trade – 60% probability of an interim deal, 2 October 2019

China Outlook – Trade war puts recovery at risk, 18 June 2019

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China's hand strengthens as US indicators nose-dive



Source: Macrobond Financial, Danske Bank

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separates the trade war track from the confrontations in all the other areas like tech, Hong Kong, NBA etc. The ceasefire between Trump and Xi in December 2018 was also made only a couple of days after the Huawei CFO was arrested in Canada on request by the US.

An interim deal should give a lift to equities and other risk assets. However, it may be short-lived as tensions are likely to continue and Chinese retaliation on the US blacklisting could remind markets that things are far from great between US and China, even if they can agree to an interim deal.

Another front opening up in US-China tensions

This week another front opened up between the US and China. **A tweet on 4 October by basketball team Houston Rockets General Manager Daryl Morey in support of Hong Kong protesters triggered a firestorm in China.** Chinese state TV and Tencent Sports suspended broadcasting of pre-season NBA basketball games and 11 Chinese companies that are official partners with NBA in China all said they halted business with the league. Basketball is *big business* in China. NBA makes at least 10% of NBA's revenues and it is expected to rise to around 20% by 2030. Nearly 500 million people in China watched NBA programs on Tencent platforms during the last season.

The case caught fire in the US as well when NBA on 7 October said in a statement that it was "regrettable" that Morey's views had deeply offended many friends and fans in China. Some US politicians attacked NBA for kowtowing to Beijing and putting "money over values". In reaction to this, the NBA responded again this time trying to appease the US audience. NBA Commissioner Adam Silver on 8 October issued a statement saying that he won't censor players or team owners over China or other issues and indicated that NBA would accept there were economic consequences of freedom of speech. This statement triggered an angry response in China again.

Comment: The case shows how the US-China tensions are broadening to people-to-people issues, and how personal views expressed by US individuals, that represent big US companies, can have economic consequences in China. It is not possible for companies to both cater to a US audience that demands freedom of speech and a Chinese audience that will not put up with insults and interference in domestic affairs.

Brace for another 'lowest growth in 30 years' headline

China will release GDP growth for Q3 next week and we should prepare for another 'lowest growth in 30 years' headline hitting the wires. Growth is set to decline to 6.1% y/y, down from 6.2% y/y in Q2.

Comment: While it is true that it would indeed be the lowest growth in close to 30 years, it is partly the **result of the structural decline in growth that China is facing**. This is a decline that all 'catching-up' economies face eventually. We expect Chinese growth rates to decline gradually towards 4½% by the end of the next decade from the current rate around 6%. However, what matters for companies is not percentage growth but absolute growth. Since China's economy is much bigger today, China adds more to the economy today in absolute terms with 6% growth than it did 10 years ago with around 10% growth. Even with growth falling to 4½% by 2030, the economy will be more than double the size at that point. And China will pass the US economy to be the biggest in the world around that time.

Chinese GDP growth set to decline to 6.1% in Q3...



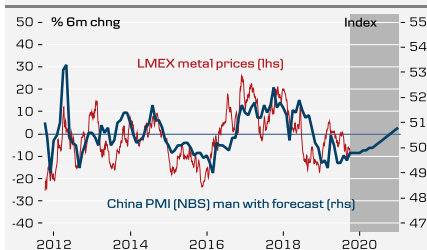
Source: Macrobond Financial, Danske Bank

... it will be lowest since 1990. That will happen many years ahead



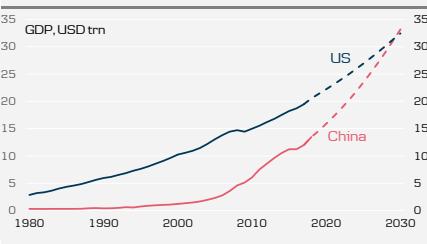
Source: Macrobond Financial, Danske Bank

Chinese growth tracker: Metal price inflation in line with moderate lift



Source: Macrobond Financial, Danske Bank

China to grow strongly in absolute terms and overtake US in 2030



Source: Macrobond Financial, Danske Bank

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