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10 May 2019

## Assessing the trade risks

### Chinese imports of goods from US and the rest of the world



Chinese imports of goods, three-month moving averages; indexed to January 2018 = 100.  
Source: China Customs, Haver

- **Trade matters:** An easing of global trade tensions is one of the key assumptions behind our call that growth in Europe will return to roughly trend in the second half of 2019. The escalation in US-Chinese trade tensions highlights the risks to that call. Just as some data (Chinese credit data, Eurozone manufacturing PMI) are starting to show that China's domestic stimulus is working and that the worst for global manufacturing could soon be over, a big round of tit-for-tat raising of trade barriers could potentially be a new shock for business confidence.
- **Donald Trump live:** Shortly after saying that a deal "is possible this week", he upped the ante. The hike in US tariffs from 10% to 25% on \$200bn of goods leaving China as of today and the Chinese threat to retaliate look like crude attempts to advance the ongoing negotiations through maximum pressure. Trump being Trump, noise could give way to a deal soon. That is and remains our base case. That the two sides are talking amid the noise is a good sign.
- **Let common sense prevail:** Logic suggests that the US and China should conclude a deal soon instead of hurling ever more tariffs or other impediments to trade at each other. Both sides have much to lose. Economic logic argues for a deal shaped more by the US than the Chinese side. The big and advanced US does not need exchange with China quite as much as the not-yet quite so big emerging market of China needs access to the US. In political terms, the cards may be stacked more evenly as the US is approaching election season. The slogan "I do deals that support jobs" would probably be an easier sell for Trump than "I wage trade wars that are hurting the US a little less than others". Balancing the economic and political logic is not easy. But is that not what negotiations are for?
- **Trade impact:** Against a modest uptrend in US trade, US exports of goods and services to China had fallen by 23% in Q4 2018 from their average for the four quarters up to Q2 2018. Chinese data on its goods imports suggest that a good deal of this reflects softer Chinese demand in general, albeit exacerbated by trade tensions, rather than direct damage from the US-Chinese trade skirmish (see chart). Also, some US exports (for example of soybeans) have simply been diverted to other markets such as the EU. Still, the divergence between Chinese imports from the US and the rest of the world suggests that trade tensions can hurt beyond their impact on confidence.
- **A lesson for Europe:** We can already draw one lesson from the current – if hopefully temporary – escalation of US-Chinese trade tensions: the next big round of trade talks, those between the US and the EU, will be noisy. By 18 May, Trump has to react one way or another to his Commerce Department's finding as to whether car and car part imports pose a threat to US national security. Whereas we do not expect him to put a blanket 25% tariff on such imports, he may reiterate the threat and possibly tie it to one of his usual ultimatums. The noise will stay with us.

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