


MACROCOSM

Extending the Tariff Deadline, Moving the Goalposts

Monday, February 25, 2019

Donald Luskin

Trump reaches to snatch more victory from the jaws of victory.

 **Donald J. Trump** @realDonaldTrump
 I am pleased to report that the U.S. has made substantial progress in our trade talks with China on important structural issues including intellectual property protection, technology transfer, agriculture, services, currency, and many other issues. As a result of these very.....
 4:39pm · 24 Feb 2019 · Twitter for iPhone

 **Donald J. Trump** @realDonaldTrump
productive talks, I will be delaying the U.S. increase in tariffs now scheduled for March 1. Assuming both sides make additional progress, we will be planning a Summit for President Xi and myself, at Mar-a-Lago, to conclude an agreement. A very good weekend for U.S. & China!
 4:50pm · 24 Feb 2019 · Twitter for iPhone

 **Donald J. Trump** @realDonaldTrump
 Very productive talks yesterday with China on Trade. Will continue today! I will be leaving for Hanoi, Vietnam, early tomorrow for a Summit with Kim Jong Un of North Korea, where we both expect a continuation of the progress made at first Summit in Singapore. Denuclearization?
 6:58am · 24 Feb 2019 · Twitter for iPhone

 **Donald J. Trump** @realDonaldTrump
 President Xi of China has been very helpful in his support of my meeting with Kim Jong Un. The last thing China wants are large scale nuclear weapons right next door. Sanctions placed on the border by China and Russia have been very helpful. Great relationship with Chairman Kim!
 7:05am · 24 Feb 2019 · Twitter for iPhone

As we expected, President Donald J. Trump announced via [two tweets](#) on Sunday afternoon that the increased level of tariffs on Chinese imports will be deferred past the March 1 deadline to allow for “additional progress” ahead of a “Summit for President Xi and myself” (see [“On the Margin: China Trade Talks at the Edge of Chaos”](#) February 19, 2019). Leave it to the [New York Times](#) to lead with this bit of snark: “Trump delayed his own deadline.”

We see this as a sign of strength – a sign that Trump believes he can get even more if talks continue, that it’s too early to take “yes” for an answer. Overnight Chinese stocks surged on the news, with the Shanghai Stock Exchange up about 6% in USD terms, bringing it 19% higher from the Trump/Xi summit in Buenos Aires. This

validates our investment thesis that China and the emerging markets in its orbit will be the prime beneficiaries of a deal (see [“Did China Just Run Up the White Flag in the Trade War?”](#) July 10, 2018, and the chart on the following page). *It encourages us in our belief that China will come out of this a stronger and more open economy, presenting both a short-term and a generational upside opportunity.*

The tariff delay could also be a “thank you” to Chinese president Xi Jinping for cooperation already given in the non-economic domain, which we have also expected. Two tweets by Trump Sunday morning suggest a connection between trade talks being seen as “Very productive,” and Xi being “very helpful” ahead of Trump’s meeting this week in Vietnam with Korea’s Supreme Leader Kim Jung-un. The tariff delay opens up time for Trump and Xi to meet personally, to seal the trade deal, and share credit on the global

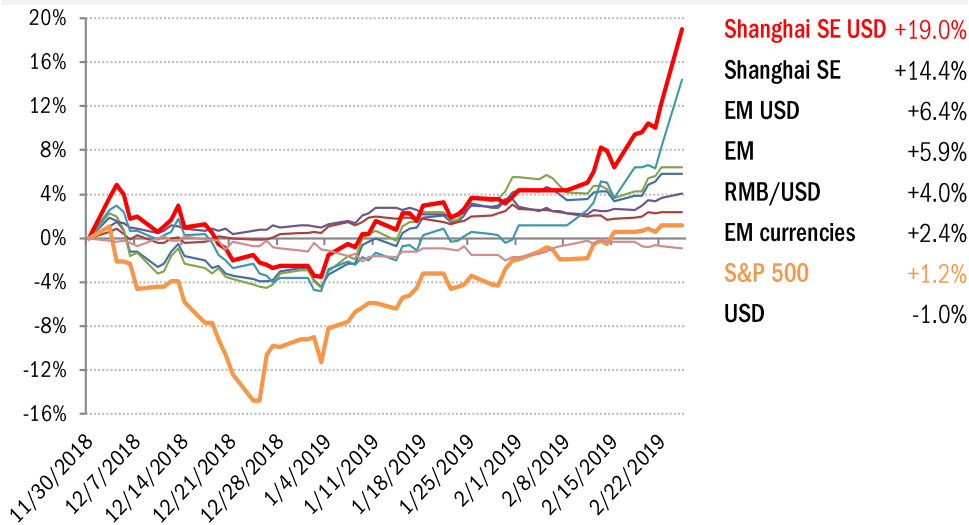
stage for it, and for working together to denuclearize the Korean peninsula.

Update to strategic view

US MACRO, ASIA MACRO, ASIA STOCKS, EMERGING MARKETS STOCKS: As we expected, Trump has extended the increase in tariffs beyond the March 1 deadline. We believe this is a sign of strength, a sign that Trump can get more by keeping negotiations going, and an indication that Trump has gotten non-economic concessions from Xi, perhaps on North Korea. The longer we have to wait for a deal, the longer China flirts with a disorderly first-ever recession, which would have global consequences. But waiting points to a more robust deal – already, it seems, concessions on currency manipulation that we thought were unattainable appear to have been won. The more a deal pushes China toward economic liberty and openness, the more a deal represents both a short-term and generational upside opportunity.

[\[Strategy dashboard\]](#)

Cumulative performance from before Trump-Xi Buenos Aires summit



Source: Bloomberg, TrendMacro calculations

- All this reaffirms our optimism that a deal can and will be done. We have pointed out often that China has been negotiating against itself ever since the Trump/Xi Buenos Aires summit, [removing its retaliatory tariffs on US autos](#), [resuming purchases of US soybeans](#), [promulgating a law eliminating forced technology transfers](#), [walking back its inflammatory Made In China 2025 program](#) – and even [starting to buy rice from the US](#) (see, among many, [“On the Margin: True Fake News on China Trade”](#) January 18, 2019). On the face of it, the only questions are: how much more can Trump get, and can the Chinese economy hold together long enough for Trump to get it (see [“Death by China on the Way to Yes”](#) December 17, 2018)?
- It is starting to look like a deal might include elements we had thought impossible for the US to obtain. Already, on Friday, Treasury Secretary Steven Mnuchin was definitive on the matter of China’s agreeing to forswear currency manipulation. Speaking to Trump about it at [an Oval Office photo op](#), Mnuchin called it “one of the areas, Mr. President, we actually concluded and reached an agreement.”
- For all this, the reflexively anti-Trump media – or, more accurately, the media whose business model depends on the constant simultaneous celebrityization and vilification of Donald J. Trump – continues to run stories like [Bloomberg’s on Friday](#), claiming that Chinese Vice-premier Liú Hè “laughed out loud” in that same Oval Office photo op, when US Trade Representative Robert Lighthizer tried to correct Trump on the meaning of the expression “memorandum of understanding.” You’re supposed to believe that the Vice-premier of China publicly laughed at the President of the United States. Not bloody likely. Indeed, the [pool video](#) of the event shows Liú, from behind, uttering a single syllable that sounds like “Huh!”, which, coincidentally, is approximately how Chinese-speakers would pronounce his own first name. This utterance came after Lighthizer had corrected something Liú himself had just said

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about memoranda of understanding, so if Liú was laughing at all, it wasn't at Trump.

- As of this writing, [a new version of that story](#) is posted at the top of Bloomberg's website, claiming that Trump and Lighthizer are "exasperated with each other" (Trump, for his part, supposedly blames Lighthizer for the stock market decline in December). Lighthizer supposedly resents Trump's "interventions." The new version of the story omits the easily fact-checkable "laugh out loud" claim.
- Sound familiar? It's the same old "[the White House is in chaos](#)" story. But that's a good thing. Remember, we've told you that big negotiations always get done at the "[edge of chaos](#)" (again, see, among others, "[On the Margin: China Trade Talks at the Edge of Chaos](#)").
- The productive chaos in deal-making isn't limited to the strife between the negotiating counterparties. It can – indeed, it almost always does – exist within each counterparty's own team, too. Smart, crafty leaders like Trump and Xi encourage this, by limiting what members of their respective teams know about the ultimate aims and limits of the negotiations. The purpose is to sow the optimal amount of confusion and fear in the mind of the opposition, by keeping one's own agents just the right amount of confused and fearful. Once everyone's mind has been sufficiently messed with in this way, the two leaders ultimately meet face-to-face as "closers" – as Trump and Xi will, probably in March, and probably at Mar-a-Lago.
- That's the deep reason why Trump can't abide Lighthizer taking any pride in the "memoranda of understanding" that have already been successfully negotiated – and in Friday's Oval Office photo op, that's what Lighthizer was doing. Superficially (but not at all trivially) any victory by Lighthizer has to be a Trump victory, and anyone whose been in politics and business as long as Lighthizer surely knows this. *More deeply, Trump is moving the goalposts to seek a more ambitious win.* By publicly carping that he needs something more solidly contractual and permanent than a mere memorandum of understanding, what he is really saying is: yes, you brought me a victory; now I want even more.
- In the aftermath, Lighthizer has done the right thing by engaging in a certain degree of groveling, [saying through a spokesperson](#), "Thanks to President Trump's firm leadership we are making strong progress on substantive structural issues." It won't disempower Lighthizer in further negotiations. Quite the contrary, his counterparties will know that no matter what they think they can get from Lighthizer, they are really negotiating with Trump.
- That's not unlike the kind of [statement Fed Chair Jerome Powell had to make](#) (see "[On the Powell/Trump Deal Memo](#)" February 5, 2019). There's no virtue in Powell not having to be politically accountable. Trump has made him a better Fed chair.
- We're only guessing when we think Xi operates this way with his people. But we do know with certainty from more than one primary source that Trump never drops the persona of wheeler-dealer, 24-by-7, constantly "playing" everyone around him with ever-changing

goals, moods and indeed entire realities. Trump is a one-man [good cop-bad cop](#) routine, a [team of rivals](#) unto himself.

- *Does he even want to do a trade deal with China? This has always been the great existential question overhanging the trade war. Does he know that making China less protectionist will just make it a bigger, stronger economy? Or is the trade war an excuse to destroy China, to end another Cold War the way Ronald Reagan ended the last one, sending his opponent spinning into economic, social and political collapse? The answer depends on the day. Indeed, it can change within the span of a single press conference* (again, see, among others, [“On the Margin: China Trade Talks at the Edge of Chaos”](#)). If his own team doesn’t know the answer, then China can never extract it from them under torture. And if you’re Robert Lighthizer, and your reputation hangs on getting deals done, then you better come up with one hell of a deal so that, once you first get China to agree with it, your own boss will too.
- For all [his claims](#) that the news media is the “Enemy of the People,” Trump must be smiling to see Bloomberg doing his bidding today, running headlines it no doubt believes are highly skeptical: [“Trump ‘Always Changes His Mind’](#)” and [“Delay Doesn’t Mean Trade War is Over”](#). The last thing Trump wants is for China, or his own team, to ever think he doesn’t always change his mind, or to imagine this trade war is over yet. It won’t be until the last second, when everyone’s hide is hanging half-way over the edge of chaos.
- We wouldn’t want to live that way. Indeed, we think much of the volatility of 2018 had to do with the market signaling it didn’t want to live that way, either (see [“2019 Outlook: Confidence Rots from the Head Down”](#) December 31, 2018).
- But for all the stories about supposedly high turnover in the Trump White House, the China negotiating team has held together without exception. And so far in 2019, in the wake of what might have been a Constitutional crisis over Trump’s possible firing of Powell (see [“On Powell in Rehab”](#) January 4, 2019), markets seem to be making their peace with it. Somehow, it seems to be working.

Bottom line

As we expected, Trump has extended the increase in tariffs beyond the March 1 deadline. We believe this is a sign of strength, a sign that Trump can get more by keeping negotiations going, and an indication that Trump has gotten non-economic concessions from Xi, perhaps on North Korea. The longer we have to wait for a deal, the longer China flirts with a disorderly first-ever recession, which would have global consequences. But waiting points to a more robust deal – already, it seems, concessions on currency manipulation that we thought were unattainable appear to have been won. The more a deal pushes China toward economic liberty and openness, the more a deal represents both a short-term and generational upside opportunity. ▶