

On the Margin: China – A Cold War with Benefits

Friday, October 25, 2019

Developing items of interest and deeper color on themes from our regular reports.

Pence's speech lays out The Trump Doctrine – it's definitely not a "truce"

Vice President Michael Pence communicates mostly with conventional speeches, like the conventional politician he is – not through seemingly improvised tweet-storms like his most unconventional boss. So the world eagerly anticipates his speeches on China, on the likely correct belief that they clearly represent the administration's *strategic* view, not its *tactical* impulses. So in [a widely-reported speech at the Hudson Institute last year](#), it seemed at first that a belligerent Pence was playing "bad cop." [His heavily anticipated speech yesterday at the Wilson Center](#) nuances that belligerence somewhat. Indeed, we could almost say that he is in some senses playing the "good cop." He lays out the strategic framework for what some are wrongly calling a "truce" in the US/China trade war. *It's actually a vision for a multi-year cold war – but one with benefits.* In contrast to the cold war between the US and the former USSR, the benefits are continued economic engagement, which are presently being re-tuned to the US's favor.

Naturally [there are media reports today](#) emphasizing China's outrage with Pence's speech – especially as it touches on China's human rights practices;



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My first thought: Pence's speech struck up the same old tune in portraying and defining China. But he spoke quite positively on improving China-US relations, saying the US doesn't want to decouple from China, and the two can and must work to share a peaceful and prosperous future.

one government spokesman said Pence's remarks "disrupt China's unity or internal stability."

But we think China's apparently official trade war tweeter, Hu Xijin, the editor of the state-controlled

Update to strategic view

US MACRO, ASIA MACRO, FX: Pence's much-anticipated China speech yesterday lays out The Trump Doctrine, a strategic outlook that denies either decoupling from China, or destroying it. It's not a truce, but a cold war – and a cold war in which there is continued economic engagement being tuned to greater US benefit. This appears to resolve the risk that Trump's real aim is to permanently disable the Chinese economy. It confirms that Trump sees the US in a multi-year struggle for trade and political reform, in which the trade dimension will remain unresolved across the 2020 election. Trump believes he will benefit from a tough-on-China platform that has already stolen elements from that of Warren; and China is complicit in providing this benefit. This slows the headlong push of China toward the cliff of a disorderly recession, and is consistent with a risk-back-on stance in global markets.

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Global Times, [captured Pence's true spirit](#): "...he spoke quite positively on

improving China-US relations, saying the US doesn't want to decouple from China."

- *This would appear, on one level, to be backing away from a cliff. It is confirmation of the risk-back-on position we have taken based on the announcement of a "Phase 1" trade deal with China (see ["The \("Phase 1"\) \(Unpapered\) \(Unsigned\) China Trade Deal"](#) October 14, 2019).*
- *There has always been a theme within President Donald J. Trump's trade war that could be understood not only as a version of "decoupling," but seeking moreover to permanently disable China's economy in order to neuter a geopolitical rival before it becomes too strong to kill. Call it a [Thucydides Trap](#) if you must – be we have always likened it to Winston Churchill's non-appeasement approach to Nazi Germany in the 1930s. This dimension of the trade war – not just the penny-ante tariffs are that being offset by currency depreciation – has always been the true risk of the trade war (see, among many, ["Death by China on the Way to Yes"](#) December 17, 2018).*
- *Now, "the Trump Doctrine" on China, as laid out by Pence, comports with our analysis that the administration is now committed to a lengthy trade war to be played out in stages, certainly crossing the 2020 US election. And it comports with our analysis that Trump will campaign by snatching Elizabeth Warren's China position from her, emphasizing reform and human rights in addition to trade, with the advantage that he will be able to claim some degree of success on trade has already been locked in (again, see ["The \("Phase 1"\) \(Unpapered\) \(Unsigned\) China Trade Deal"](#)).*
- *In this sense Trump sees an ongoing struggle with China as a political benefit, and it appears to be one with which China is willing to cooperate.*



game on "social justice," but [kowtow](#) to Chinese pressure in order to

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preserve their revenues. But the strategic essence of his speech is in these passages (with our emphasis):

“When Deng Xiaoping’s ‘Reform and Opening’ policy encouraged engagement and exchange with the outside world, the United States responded with open arms. We welcomed China’s rise. We celebrated the remarkable accomplishment of 600 million people lifting themselves out of poverty. And America invested more than any other nation in China’s economic resurgence.

“The American people want better for the people of China. But in pursuit of that end, we must take China as it is, not as we imagine or hope it might be someday.

“And people sometimes ask whether the Trump administration seeks to ‘de-couple’ from China. The answer is a resounding ‘no.’ The United States seeks engagement with China and China’s engagement with the wider world, but engagement in a manner consistent with fairness, mutual respect, and the international rules of commerce.

“But, so far, it appears the Chinese Communist Party continues to resist a true opening or a convergence with global norms.

“All that Beijing is doing today, from the Party’s great firewall in cyberspace or to that great wall of sand in the South China Sea, from their distrust of Hong Kong’s autonomy, or their repression of people of faith all demonstrate that it’s the Chinese Communist Party that has been ‘de-coupling’ from the wider world for decades.”

These words are not the stuff of “truce.” But, happily for markets, neither are they the stuff of deliberately pushing China off a cliff, and never mind the consequences for the global economy. We can’t think of a better word for it than “truce,” though – we need a word that doesn’t suggest the fighting has stopped, only that it’s not intensifying. The closest we can come is “cold war.”

- The tariffs already in place – which China has paid for with currency depreciation – will stay in place until and unless China pays to remove them by agreeing to reforms.
- New tariffs, announced but so far not implemented (see [“On the New China Tariffs”](#) August 1, 2019), won’t be implemented so long as China signs onto “Phase 1.”
- The Trump administration will continue to put diplomatic pressure on

Chinese human rights issues, but without overtly inciting protestors or making it personal with President Xi Jinping.

- China will continue to feel growth pressure because Trump has succeeded in [changing the conventional wisdom about China as a place to do business](#). Concerns like Nike and the NBA won't disengage from the Chinese market very quickly or very much. [Former NBA star Charles Barkley said yesterday](#) that Pence "needs to shut the hell up" because "All American companies are doing business in China." But at the margin, things are changing. As another former NBA great [Shaquille O'Neal said Tuesday](#), before Pence's speech, "...we do a lot of business in China," but "... Whenever you see something wrong going on anywhere in the world, you should have the right to say, 'That's not right.'" It's not just sports-talk. Apple has already [moved some i-Phone production to India](#), and plans more non-China production diversification. We think few businesses will seek *new* presence in China, nor expand their facilities in China, while so much business and moral uncertainty exists. For a capital investment-driven economy like China, such pressure on growth is very salient, and will keep China at the negotiating table.

This isn't grounds for an all-clear signal on the risk of China being pushed over a cliff into a disorderly first-ever recession. But the sprint toward that fog-hidden cliff has been slowed to a walk, and that's all to the good.