Supplement to *Here Comes the Sun*
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China's Initial Agreement as Part of the Temporary Trade Truce

As part of the agreement, China pledged to:

- Significantly increase its imports of energy and agricultural products from the U.S.
- Expand trade in manufacturing goods and services, including financials, healthcare, education, and business services
- Strengthen protection of intellectual property rights (IPR)
- Enhance bilateral investment

The beauty of this negotiation outcome for China is that it focuses on the economic complementarity between the two countries; reducing the U.S. trade deficit seems to be coming from sending more exports to China rather than greater restrictions on China's exports to the U.S. The former is much less disruptive than the latter.

So What Could China Buy?

The focus will be energy, agricultural, and some manufacturing goods and services. We expect China's current account surplus will continue to narrow. This is an overview of the current exchange of goods and services, and where we believe there could be improvement:

- In 2017, China imported $200bn worth of energy products at 13% year-over-year (YoY) growth—only $6bn is from the U.S. China imported $94bn of agricultural products at 43% YoY growth, with only $20bn from U.S. So there is a lot of room to grow the U.S. share.
- China's share in U.S. beef exports was merely 0.3% in 2017, and only 1.4% of China's beef imports came from the U.S. In contrast, room for further increases in soybean imports from the U.S. could be limited, given that China already took 63% of U.S. annual soybean exports last year.
- From a complementary perspective, chemicals, aerospace, non-electrical machinery, and high-tech products have potential, as they are the key U.S. products with comparative advantage, while their export share to China is still relatively small. However, U.S. will not allow China to buy more high-tech product, hence only the others are available as options.
- In 2017, China's beef imports increased by $10bn and imports of liquefied natural gas (LNG) increased by $9bn. China's total imports of aerospace, chemicals, and non-electrical machinery increased by $50bn, while imports of high-tech products rose by $40bn. So if China's incremental import growth shifted to the U.S., the number has the potential to grow to $70bn or so.

Trade Tariffs Escalate on June 15

On June 15th, the United States Trade Representative (USTR) released a list of Chinese products that would be subject to additional tariffs. The list consists of two parts. The first part is a sub-list of 818 products from the original list of 1300+ products issued in April, worth about $34 billion. Tariffs on these products will be levied starting on July 6. The second part of the list consists of 284 additional products worth $16 billion, to be reviewed in a public notice and comment process further. The USTR's final list includes 1,102 product lines including robotics, aerospace, industrial machinery, and automobiles. Not included are consumer goods including mobile phones and televisions. The move is a response to the USTR's Section 301 investigation earlier this year that accused China of stealing U.S. intellectual property. China's State Council announced it would levy penalties of the same rate on $34 billion of U.S. products, covering 545 categories, ranging from soybeans, pork, chicken, and seafood to sport utility and electric vehicles. The remaining $16 billion of products are to be reviewed later. Including farm goods was targeted toward Trump's voter base. In addition, all previous agreements achieved during earlier negotiations will be invalidated.