

Trade week

China and the US resume talks on trade this week - there is some optimism, but this has often in the past been misplaced



A narrow deal?

It looks as if we are back to considering the merits of a narrow trade deal today, as news stories break suggesting that China is not looking to make a broader trade deal along the lines it is reported the US is seeking.

I'm intrigued by this, as from a strategic point of view, I would have thought that the US would have the most to gain from a partial deal, not China.

1. The US economy remains in fairly good shape, but recent data show that this position is being undermined, in particular by trade-war-affected manufacturing;
2. The US economy has further to fall, and perhaps has fewer stimulus policies up its sleeve
3. The benefits of fighting China on trade may now be being outweighed by the short term hit to the economy, in terms of popular support and potential votes for President Trump at next year's Presidential election
4. Given the points above, China may see it as advantageous to keep the trade war alive, but under control pending political developments in the US.

What may undermine these strategic considerations in the short term is the impact that swine fever is having on pork-supply in China and the need for other agricultural goods such as soy. Even

if the strategic points above are correct, feeding the nation clearly will always come first, so this may be the dominant thinking this week.

A mutual olive branch from the US could be further delaying the implementation of the most recently announced tariffs.

Against this, the US has indicated that it wants a broad-based deal. Nothing is yet in the bag, and optimism on trade has proved time and again to be misplaced.

US data - supports Fed cut, but could have been worse

As James Knightley (JK) [writes in the linked note](#), the US jobs data last Friday raise the prospects of a further Fed rate cut (house view is another at the 31 Oct meeting and then again in December). But the data could have been considerably worse, at least from a risk asset perspective.

One of the things JK has been highlighting recently is the sharp pick up in wages and core CPI. On an annualized basis, this has been looking particularly worrying. But if we have learned anything about US wages (indeed wages globally) since the financial crisis, it is that just as they begin to look worrying, they are either revised lower or simply fall back. This seems to be the world we live in. It doesn't matter how tight the labour market gets, how low the unemployment falls (now only 3.5%), we just don't seem to get wages blowing out. Before moving to Asia, I spent years wrongly worrying that we were on the verge of US wages finally bursting up. Almost three years later, they still haven't. I'm not sure now that they ever will.

But this is potentially not as bad as it looks. Face it, had wages been hurtling higher, as growth stagnated, it would have tied the Fed's hands to respond. At least this way, there is little to stand in their way on 31 October. And that should provide a modicum of comfort to equity investors.

One brief aside, in terms of US labour tightness, I had two weeks of marketing in the US recently. My unofficial benchmark for how tight the US labour market is has for many years been based on the quality of service in fast-food outlets. The relationship is inverse. If you get your order rapidly, and accurately, there is slack in the labour market. The Fed has ample room to move. If your order is completely wrong, and given to you with an accompanying "Killer accent dude!", it is tight, and the central bank in question has limited room.

My observation: It is tight, very tight...

Brexit - election first! After which...?

There seems little chance that PM Johnson's "compromise" offer to the EU on the Irish Backstop has a hope of being passed, or even that it will form a broad "landing pad" for an EU counter-offer. There is some chat about a further offer from the UK before this Friday. That would indicate that the current government is actually serious about getting a deal. This is not clear.

[James Smith covers this all in great detail here](#). Note, the Brexit deadline is 31 October, but 19 October is the effective deadline, after which, according to the Benn bill passed in September, the PM will have to ask the EU for an extension to article 50.

And then, and probably only then, we may expect a vote of no confidence and a General Election.

What happens then is anyone's guess. A variety of polls indicate that a second referendum would

narrowly be won by "remain". But to get a referendum, we would need a broad coalition of Labour and Liberal Democrats and probably others to form a government. At the moment, the Conservative Party is ahead in the polls. If they campaigned on a "no-deal" ticket, forcing out the Brexit Party, then they could possibly win a majority under the UK's first-past-the-post system, which would mean that the UK might still be leaving, and without a deal.

It's probably time for me to contact the British Consulate and arrange for my postal vote (though I often worried that most of these ended up in the bottom of the Regent Canal).

In the meantime, expect GBP to swing widely.

Week ahead

In the week ahead in Asia, Prakash Sakpal writes: "Malaysia's 2020 Budget due on Friday is expected to focus on growth. The Malaysian economy will find it increasingly tough to continue to outperform the global slowdown as external headwinds from trade and the tech war are gaining strength. As such, we expect the budget to include some growth-boosting measures, keeping the deficit above 3%." (For more, see our [Asia Week ahead publication](#))

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