Investment Strategy Update

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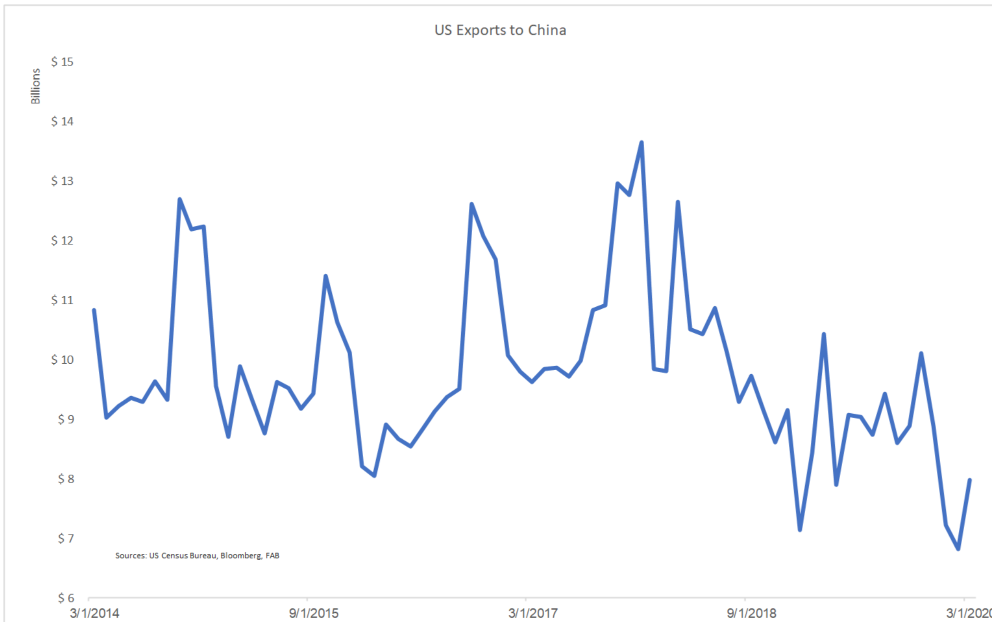
US-China trade deal could become a victim of Covid-19

♦ **China says it has halted some imports from the US in retaliation for the country's stance on the new Hong Kong law.**

♦ **China had already signalled that the economic downturn in the country because of the Covid-19 lockdown would impair its ability to meet its commitment on purchases of US products.**

♦ **President Donald Trump is focused on protests at home but could soon turn back to China as election nears.**

♦ **FAB AAC remains underweight in equities and overweight in gold.**



Much of the news attention has been on the protests raging in the US and the potential for more protests in Hong Kong, but investors are starting to realize that they soon might have to discount the end of the preliminary trade agreement between the US and China too. Today, Beijing said that it would pause importing some US products including soybeans.

President Donald Trump is likely to take the announcement personally, given that US farmers have been among his strongest supporters, even after they suffered falling prices and exports during the height of the trade war last year. The decision also comes at a time when his administration faces the worst civil unrest since 1992, with violent protests rocking the country from Minneapolis to New York.

In such an environment and with the November elections less than six months away, President Trump could feel compelled to raise the rhetoric a couple of notches. The trade deal is an obvious target for President Trump, given that he saw how much damage his tariffs caused to China in the past two years.

While that may unsettle markets, there is a growing chance that the trade agreement will be scrapped by the time it comes up for a review in October anyway. China has already warned that it may not be able to meet the US requirement that it buy US$200 billion in American goods this year given the Covid-19 crisis. Indeed, Chinese imports from the US have actually dropped this year instead of increasing.

Markets have taken increased risks in stride as new stimulus continues to be piled into the system, the latest coming from Europe. Investors have also focused on the positive signs that the world economy is recovering as it reopens. Today, China's Caixin manufacturing PMI came in above 50, a level that indicates expansion, suggesting that factories in China are increasing output again.

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Similar measures in Europe also showed marked improvement, though most remained below the 50 mark. The protests and the louder tone between the US and China, however, are a reminder that the collateral damage from the global lockdown that resulted from the Covid-19 pandemic is extensive.

For the time being, a wall of cash is keeping asset prices supported and is likely to make any sell-off short-lived. Yet, as people take to the streets from Hong Kong to Chile and the US, investors eventually will have to come to terms with the fact that liquidity alone cannot fuel economic growth. And without more production of goods and services, asset prices cannot keep rising forever.

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