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Making sense of the big, beautiful monster trade deal: Part #4

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As we discussed in Part #1, the long-awaited details of the Phase 1 trade deal between China and the United States were released on Wednesday, January 15, 2020. The Agreement called a "big, beautiful monster," has extensive detail in some areas and others are left rather vague. In this final Alert (Part #4), we examine the Agreement's chapters related to financial services regulation, macroeconomics/currency exchange rates, and dispute resolution.

Financial services

National Public Radio reported directly after the Agreement was signed, "One winner in the new U.S.–China trade deal is the U.S. financial services industry. Bankers, investment firms, and insurance companies would have more access to the world's second biggest economy." Indeed, the Agreement builds on the work started many years ago to open up China's economy for financial services companies. We wrote an Alert last July where we described, "In November 2017, China first announced a plan to allow foreign companies to own financial services businesses in China. That plan called for allowing ownership of 51% of financial firms in three years and the removal of all restrictions in five years. In 2018, that timetable sped up to allow foreign companies to own 51% of these businesses in that year and lift ownership restrictions in 2021."[1] We reported back then that Chinese Premier Li Keqiang announced, "We will achieve the goal of abolishing ownership limits in securities, futures, [and] life insurance for foreign investors by 2020, a year earlier than the original schedule of 2021."

The current Agreement lays out some details on the expanding access by American companies in this sector. China agreed, "Within five months after the date of entry into force of this Agreement, China shall allow branches of U.S. financial institutions to provide securities investment fund custody services, and the parent company's overseas assets shall be taken into consideration in order to fulfill applicable asset requirements." Other access to the China market will, according to the Agreement, also take into account U.S. companies' ***global presence*** in providing qualifications.

[1] See "What trade trouble? China opens up its financial services sector earlier than expected and other reforms," available here.

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The Agreement specifically calls for allowing other U.S. credit rating services to be allowed to operate in China. Currently only one wholly U.S.-owned service—S&P—has been granted a license. But, China is to open up their market to more services in three months. China also is specifically agreeing to ease up on U.S. credit card companies, "including any license application of Mastercard, Visa, or American Express." In addition, China is agreeing to greater access in

- distressed debt;
- insurance services; and
- securities, fund management, and futures services.

This access is to be accomplished through reducing or eliminating ownership restrictions, streamlining application procedures, and technical changes.

Under the Agreement, the U.S. does promise to provide reciprocity, including supporting access to the American market for CITIC Group, Union Pay, China Reinsurance Group, and China International Capital Corporation specifically.

Currency exchange

The U.S. has long accused China of manipulating their currency—the yuan or renminbi—to benefit their trade program—branding China as a currency manipulator. U.S. Treasury Secretary Steven Mnuchin described the U.S. theory in September of last year, "If the RMB depreciates 15 percent and you put on a 15 percent tariff, that means that U.S. companies can buy in dollar items 15 percent cheaper." Mnuchin also used that theory to promote the president's belief that Chinese business and not U.S. importers were paying for the tariffs.

Two days before the Agreement was signed, the U.S. removed the "currency manipulator" moniker from China. The Agreement itself calls on the parties to refrain, "from competitive devaluations and not target exchange rates for competitive purposes, including through large-scale, persistent, one-sided intervention in exchange markets."

Dispute resolution

The final section of the Agreement deals with evaluating the progress of the deal and resolving any disputes that may occur over time. While it does lay out a structure for this process, the details of what constitutes a breach of the Agreement are left very vague and the mechanism for enforcement is also unclear—beyond simple retaliation. The Agreement does set up a Trade Framework Group in which both parties will meet at least every six months to "discuss the implementation of this Agreement." It also establishes Bilateral Evaluation and Dispute Resolution Offices in each country to manage the day-to-day issues. If good faith efforts fail to resolve disputes, the parties can retaliate "by suspending an obligation under this Agreement or by adopting a remedial measure in a proportionate way that it considers appropriate with the purpose of preventing the escalation of the situation and maintaining the normal bilateral trade relationship."

Conclusion

More important than any of the details (which are lacking) of the trade deal, the fact that the spirit of the Agreement is one of bilateral cooperation instead of mutual antagonism is most significant. The Chinese and American governments stepped away from the brink of all-out trade war and have

laid out a path forward for the massive economies to co-exist and perhaps work together. The lack of specifics makes it difficult to assess the real economic benefit to American industry and, moreover, any particular U.S. business. However, there is enough potential for opportunities that should draw the attention of companies from the U.S. looking at doing business in China.

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