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Weekly Wrap: G20 Outcome Hinges on Trump-Xi Relationship; A Red Line on Iran

Week in Review – A Trump-Xi phone call alleviated some uncertainty about the prospects of a meeting at the G20 next week. We are now watching a speech by Vice President Pence and a report due next week outlining threats to U.S. telecoms networks as potential threats to the ultimate outcome of the meeting. Retaliatory strikes against Iran after the downing of a U.S. drone were called off, but the threat of escalation inches closer.

Looking Ahead – We view a delay in tariff implementation on \$300 billion Chinese goods as a likely (but not given) outcome of next week's G20 negotiations. The Democratic Presidential debates kick off next Wednesday that may impact markets as ambitious policy proposals on healthcare, tax policy, education, and others are introduced to a broad national audience.

THIS WEEK IN WASHINGTON

Previewing G20 expectations after Trump-Xi meeting confirmed. Presidents Trump and Xi are set to meet for an “extended meeting” next week at the G20 following a phone call between the two leaders. While this is clearly a positive development, we caution that we have seen positive sentiment cast around China trade developments by Trump and other officials while the underlying negotiations trended negative behind the scenes, highlighting the ever-unpredictable nature of these talks. A speech by Vice President Pence next Monday (June 24) now becomes even more of a focal point, as a less confrontational tone or a rescheduling of the speech altogether would be a clear sign of good faith. The last meeting of the two leaders in December 2018 led to a three-month delay on a tariff hike to 25% on \$200 billion of goods, and the current state of talks makes a similar result the most likely outcome for the next negotiating round on June 28-29.

Although near-term indications are trending to a more market-positive result, the expanded scope of the trade fight at this juncture may make it harder to come to any sort of agreement, even in the form of a delay. In the event of a good meeting that leads to a potential 90 day delay on tariff implementation, the chances of a full 25% tariff on \$300 billion of additional Chinese goods likely drops to near zero for the near-term, but the threat of the tariffs being implemented longer-term is approximately 40%. We may still see some sort of tariffs levied on this tranche of goods at some point, but they would likely start off lower (perhaps at 5%) and gradually raise to create additional inflections points in negotiations.

If the meeting produces a negative outcome, we see a 75% chance that Trump moves quickly to implement further tariffs on the \$300 billion of goods on or around July 1. However, we expect that the initial tariffs would not be set to the highest 25% rate. More here: [FAQ's on China Trade Ahead of Next Week's G20 Meetings](#)

Trump signals weariness on military confrontation with Iran. The Trump administration has effectively drawn a red line following the latest flare-up that saw the downing of a U.S. drone by Iran. A strike against Iranian targets in retaliation was confirmed to have been called off by the President last minute to avoid escalation over the loss of strategic equipment that did not endanger U.S. soldiers in the area. A demonstrated readiness to strike back that emphasizes the safety of U.S. personnel has been communicated by the administration, but heightened tensions elevate the risk of miscalculations that will continue to pose a threat over the coming months barring a move towards diplomatic discussions. As we highlighted last week, the latest action by Iran drawing a U.S. response comes as uncertainty in key defense positions continues. Acting Defense Secretary Pat Shanahan is stepping away from his role, leaving the Defense Department without a permanent head since the departure

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of Secretary Mattis in December 2018.

Facebook's cryptocurrency announcement draws heavy scrutiny from lawmakers. The announcement of Facebook's "Libra" cryptocurrency project has refocused lawmakers' attention on the company compounded by existing concerns about privacy violations and anti-competitive practices. Lawmakers are skeptical about Facebook's ability to maintain appropriate safeguards around financial data and adequately prevent illicit financial transactions already ripe in the cryptocurrency environment. A skepticism already exists on Capitol Hill about the intertwining of commerce and finance, but the current sentiment around reigning in "big tech's" influence is further fueling pushback. House Financial Services Committee Chair Maxine Waters called on Facebook to stop Libra's development and Senate Banking Committee Chair Mike Crapo announced a hearing to examine the project on July 16. Although we do not expect any legislative steps to be taken to reign in Facebook's development of the cryptocurrency, lawmakers will apply significant pressure to publicly demonstrate oversight over the industry's expanding reach.

An interview with HHS Senior Advisor for Drug Pricing John O'Brien. HHS Senior Advisor for Drug Pricing John O'Brien participated in a fireside chat at the Raymond James Life Sciences and Med Tech Conference in New York. As can be viewed in our [recap](#), our biggest takeaways were: 1.) the drug rebate rule is progressing with a soft target of January 1, 2020; 2.) proposals around drug importation are moving forward and drugs produced at sole source facilities for international and U.S. versions could be targeted first; 3.) if the Speaker offers up a drug pricing plan that includes direct pricing negotiation, it will likely be DOA in the Senate; 4.) Mr. O'Brien expressed skepticism that HHS should negotiate drug pricing for Medicare; and 5.) Mr. O'Brien took a cautious view on the Medicare Part B IPI, stating that the Administration was still reviewing the comments that were received.

Positive progress on USMCA. Mexico's Senate has ratified the USMCA and USTR Lighthizer confirmed his openness to addressing Democrats' desired changes in implementation language in the latest positive developments on the agreement's progress. The Trump administration continues to push for a final vote on USMCA sometime before the August Congressional recess, but it will be difficult to achieve at this point given that there are only 16 legislative days remaining after this week. Key catalysts we will be watching for is agreement between USTR and Congressional Democrats on implementation legislation and the introduction of the legislative text, which will trigger the 90-legislative day timeline for passage under Trade Promotion Authority (TPA).

The Trump v. Powell friction continues – but Trump lacks support to replace Fed Chair. Reports emerged this week ahead of the Fed's rate decision that President Trump explored the possibility of demoting Fed Chair Powell, but the speculation largely misses the fact that the Senate would not approve a replacement. Powell has broad political backing and a nominee would have to clear the Senate, largely precluding the possibility that a nominated replacement would get the necessary votes for confirmation. Powell's tenure runs through February 2022 and Powell has confirmed his intention to finish out his term. The continued friction between Trump and the Fed may provide Trump with some flexibility to cast off blame for any economic slowdown as the election cycle ramps up given his repeated calls for lower rates to sustain the economic expansion.

WHAT'S AHEAD

Stage set for Democratic debates – what to watch next week. The emerging Democratic candidate field offers a preview of a coming primary process that will be much bolder in terms policy ideas compared to 2016 as candidates seek to redefine the identity of the party. The sheer number of candidates (currently at 23) lends itself to an ideas-based/attention getting campaign as a means of differentiating early from the rest of the pack. Broadly speaking, some of the proposals we've seen so far are not incremental, middle-of-the-road adjustments to the current status quo – rather wholesale reforms of established systems. Eliminating private health insurance in favor of government-sponsored "Medicare-for-All," breaking up "Big Tech" companies, free college tuition, and providing nearly a \$3 trillion middle-class tax cut are just some of the opening talking points of the more prominent Democratic candidates.

There will be friction within the party on the appropriate path to uniting Democratic voters. We are seeing some candidates pledging to focus on pragmatic ideas that resonate with a broad electorate, while others see value in running in opposition to President Donald Trump and his policies – speaking to the core party base.

Democratic victories for contested House seats and governorships in the 2018 midterm cycle may hint at the preference of the national electorate for opposition candidates to the current incumbent. Democrats flipped 41 seats in the House to take the majority, with more than half of the ousted Republicans coming from Congressional districts won by Trump in 2016. Successful candidates in some of the more competitive races leaned more moderate; were young and relatively new to politics; and were, in many cases, women. Of the 20 Democratic candidates we will see on the first debate stage, eight are 50 years or under, six are under 45, and six are women – marking one of the youngest and more diverse fields of candidates.

Graphics giving an overview of the candidates appearing in the first debate and a schedule of state primaries is available here: [Previewing the 2020 Democratic Primary](#)

Dems and White House no closer to budget deal. Negotiations between the White House and Congressional Democrats on a budget agreement have not led to a breakthrough following another round of talks earlier this week. Domestic spending levels continue to be the major barrier, but positive signs are emerging that both sides are working to avoid mandatory spending cuts that will be triggered at the end of September. A shorter-term continuing resolution on spending levels and an extension of the debt ceiling is on the table, but we ultimately believe a two-year deal that raises spending and takes the debt ceiling question out of the equation during the 2020 election season will be reached sometime later this summer/early fall. The House is prioritizing and voting to approve spending bills that will continue to put pressure on the White House/Congressional Republican leaders to reach a deal with Democrats focusing specifically on spending increases for domestic priorities.

Romney amendment to curtail Trump's influence on China's tech national security threat. An amendment introduced this week by Senator Romney to the National Defense Authorization Act (NDAA) would stipulate the conditions under which Huawei could be removed from the Commerce Department's entity list that limits U.S. component exports. If successful, the amendment could complicate the question of the Huawei effective ban being addressed in current trade negotiations and highlights Congressional desire to separate tech national security considerations from ongoing trade talks. The development also signals that oversight over threats posed by China's tech to the U.S. will not subside in the event of a trade deal. Lawmakers have criticized the President's reversal of last year's ban on ZTE, arguing that national security should not be used as a bargaining chip in U.S.-China negotiations.

[DATES TO WATCH](#)

June 24: (expected) Vice President Pence speech on U.S. policy towards China

June 24: President Trump ceremony to announce executive order around provider transparency

June 25: House Energy and Commerce Health Subcommittee hearing titled "Reauthorizing Vital Health Programs for American Families"

June 25: CFPB conference on defining "abusive acts or practices" for UDAP enforcement

June 25: House Financial Services Committee hearing on fintech regulation

June 25: Senate Banking Committee hearing on potential systemically important financial institution designation for Fannie Mae and Freddie Mac

June 26: Senate HELP Committee markup for Lower Health Care Costs Act

June 26: Senate Budget Committee hearing on reforming federal budget and spending process

June 26-27: Democratic Presidential Debates, Miami FL

June 27: Release of Fed's Comprehensive Capital Analysis and Review (CCAR) results for banks

Week of June 24: Finalization of report by Director of National Intelligence on foreign threats to U.S. networks, per White House national emergency declaration

June 28-29: G20 Summit Tokyo; scheduled meeting between Presidents Trump and Xi

Late June/Early-Mid July: Expected introduction of USMCA implementation language, triggering 90-day timeline to final vote

July 16: Senate Banking Committee Hearing on Facebook's "Libra" cryptocurrency

July 23: Senate Judiciary Committee tech/antitrust hearing

Expected Late July/Early August: Administration decision on tariffs on \$11 billion EU goods in Airbus subsidy dispute

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