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Trump-Xi Summit: Trade Truce, AI Race

More details are emerging on the upcoming Trump-Xi summit. President Trump and President Xi are expected to meet in Washington, with most of the agenda scheduled for 24-25 September. Their discussions are likely to focus on three areas: trade, AI and national security. Despite US-China disagreements at the G20, we are more constructive on this summit than we were ahead of the May meeting. The recent intensification of exchanges between senior US and Chinese officials has further reinforced our view.

The near-term outlook for bilateral trade appears increasingly positive. An extension of the trade truce, additional Chinese purchases of US products and a reciprocal tariff-reduction package would help sustain the current double-digit growth in China-US trade, reinforce tailwinds for the renminbi and provide a buffer against China's slowing domestic growth.

By contrast, strategic competition, particularly in AI, will probably persist amid a winner-takes-all mindset. Sustained AI competition is likely to add to capital-expenditure pressures and intensify demand for power and infrastructure. This could push up yields at the belly and long end of UST and CGB curves over the next couple of years, particularly in the US, given its economy's greater sensitivity to inflationary pressures.

Beyond trade and AI, China may be increasingly willing to position itself as a mediator between the US and Iran as the conflict in the Middle East risks further escalation. With fuel inventories at Chinese state-owned enterprises running low, China would still benefit from reduced disruption to global energy supplies. Moreover, an easing of US-Iran tensions would also reduce China's exposure to US secondary sanctions and, in turn, the risk of renewed tensions between China and the US.

Trade: The Clearest Area for Progress

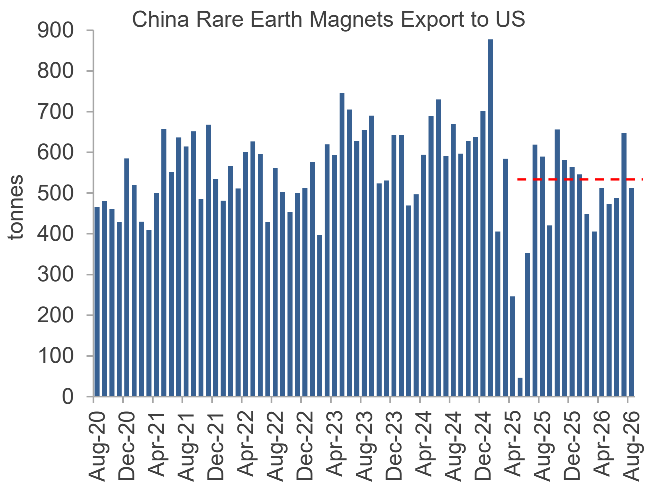
China and the US are likely to extend the current trade truce for another year or so, alongside a further easing of China's restrictions on rare-earth exports and increased Chinese purchases of US agricultural and energy products. In return, the US may remove some Chinese companies from its sanctions lists.

There is also a meaningful possibility of bilateral tariff reductions. China's Ministry of Commerce has confirmed that negotiations are under way on a US$30bn reciprocal tariff-reduction package. Vice Premier He Lifeng met US Treasury Secretary Bessent and US Trade Representative Greer last Sunday to lay the groundwork for the summit.

Recent data already point to a significant stabilisation in US-China trade relations. Bilateral trade growth has returned to double-digit rates since April, reversing the contraction recorded a year earlier (Fig. 1). Despite significantly higher prices, China's rare-earth exports to the US have largely recovered to pre-Liberation Day volumes (Fig. 2). Moreover, Chinese state-owned firms' orders for US soybeans have begun to gather pace in recent months, despite the additional 10% tariff. Taken together, these developments suggest that both governments have incentives to preserve the recent improvement in trade flows and reduce the risk of renewed trade confrontation.

Fig 1 Double-digit increases in China-US trade value

Fig 2 China's rare-earth exports have remain relatively stable



Source: CEIC, Bloomberg, Mizuho

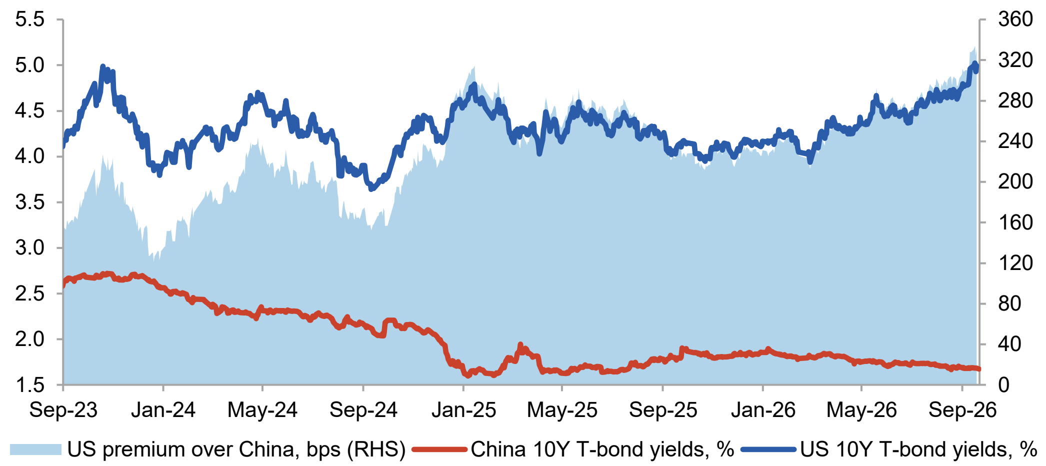
AI: The Main Area for Strategic Competition

The summit is unlikely to produce meaningful cooperation or agreement on guardrails for AI development. The US retains a clear lead in frontier models and advanced semiconductors. China, however, has important advantages in lower-cost open-weight models and a more secure nationwide power network. Neither Washington nor Beijing appears willing to slow down as the AI race intensifies.

Although executives at leading US AI companies have called for a slower pace of development, citing potentially serious risks, President Trump has rejected this approach and emphasised the importance of maintaining the US lead over China, arguing that "whoever wins AI, wins." US Treasury Secretary Bessent has similarly warned that "there is no day after tomorrow" if the US loses the AI race, in view of growing opposition to data-centre construction across US communities.

This is not only a contest for technological leadership and infrastructure. It is also becoming a race for capital. As Anthropic and OpenAI consider potential listings, China's DeepSeek has reportedly begun preparations for an IPO on Shanghai's STAR Market. While the timing and fundraising target remain uncertain, a 2027 listing appears increasingly plausible. The scale of AI-related investment, particularly in the US, could add to overheated capital demand and exert further upward pressure on long-dated US Treasury yields (Fig. 3).

Fig 3 The resilient rise in US treasury yields is incrementally slowing the US in the capital race



Source: Bloomberg, Mizuho

That said, China and the US may agree to establish a notification mechanism in the event of a major AI accident threatening national security. Such a mechanism would primarily aim to prevent accidental escalation during an AI-related crisis. It is also possible that both parties could agree to work towards a global AI governance framework resembling the international regime governing nuclear weapons, although such a framework would probably take years, rather than months, to establish.

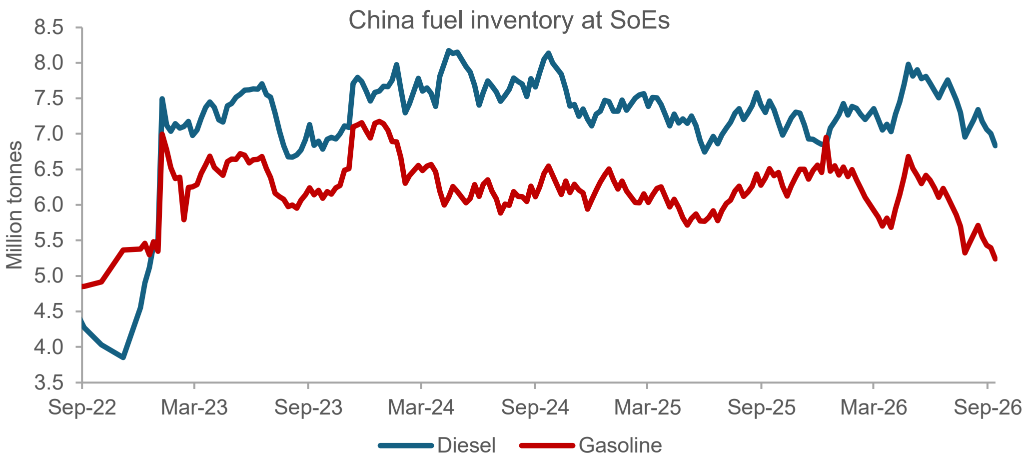
Geopolitics: China as a Mediator?

China may be more willing to position itself as an intermediary between the US and Iran, as the conflict in the Middle East risks further escalation. While disruptions in the Strait of Hormuz are entering their eighth month, the Houthis have also positioned forces near the entrance to the Red Sea. Last week, Chinese Foreign Minister Wang Yi held talks with Iranian Foreign Minister Seyyed Abbas Araghchi before speaking by phone with US Secretary of State Rubio the following day. Even so, any joint US-China statement criticising Iran or pressuring it to return to peace talks remains highly unlikely.

Admittedly, the renminbi has been relatively resilient amid heightened tensions in the Middle East and was, for a period, the only Asian currency to appreciate following the outbreak of the conflict. That said, China would benefit more in the long run from orderly global supply chains and reduced energy-market disruption.

Recent data suggest that gasoline and diesel inventories at Chinese state-owned enterprises are running low following strikes on refinery facilities in the Middle East and Russia (Fig. 4). An easing of US-Iran tensions would also reduce the risk of China being exposed to US secondary sanctions.

Fig 4 Gasoline and diesel inventories at Chinese SoEs are running low in this extended US-Iran conflict



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