Week in review
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In this week's update, Kevin Quinn discusses:

- US-China trade deal
- US inflation
- US trade deal with Saudi Arabia
- US dollar rebound
- President Trump's "One Big Beautiful Bill"
- Germany's military plans
- UK economic growth
- Moody's downgrade US credit rating

Latest update from markets (to 16.05.25)

	Past week	YTD
Global shares	+5.1%	-2.2%
US shares	+6.4%	-5.5%
European shares	+2.4%	+10.4%
European government bonds	+0.0%	+0.1%
Global commodities	-0.75%	-5.1%
The Magnificent 7*	+10.5%	-11.0%

Source: Bloomberg, 19.02.25. All returns expressed in euros.
*Apple, Alphabet, Amazon, Meta, Microsoft, NVIDIA, and Tesla.

The long and short

Investing requires a long-term focus but shorter-term events can take most of our attention. In these weekly updates, we place current events into a longer-term perspective.

The long…

US tariffs and the "Overton Window"………

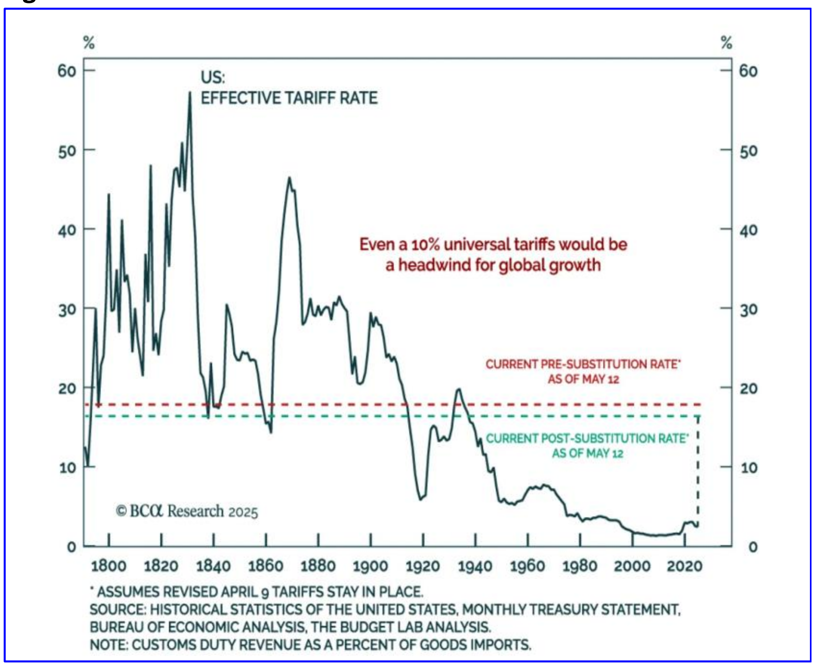
The "Overton Window" is a model for understanding how ideas in society change over time and influence political decisions. The model's basis is that politicians typically support policy ideas that are widely accepted by voters. These policies lie inside "the Overton Window".

The window changes over time either increasing or decreasing the number of ideas politicians believe they can support without risking losing voters' support. It is rare for a politician to move the window themselves, as more often the model reflects a slow evolution of societal values and accepted norms. **It appears not so though with President Trump and his tariff policy.**

Since January 2025, when the effective US tariff rate[2] stood at 2.5%[1], the Overton Window has moved into levels not seen in the past century[1]. Prior to the US-China trade agreement earlier in May, 145% US trade tariffs on China had effectively meant a trade embargo[3] was in place between the world's two largest economies.

US tariffs going forward

Figure 1: US effective tariff rate since 1776



Source: BCA Research 12.05.25

What Figure 1 above from BCA Research tells us is a simple story, US tariffs will most likely be at levels not seen since 1941. As a result, the Overton Window has shifted with US voters, investors and markets now accepting a level of tariffs many multiples higher than 2025 began with.

The question today is whether the most recent rally by equity markets in response to the US-China trade deal can hold?

What we know for sure is that we are past peak US-China tariff risks and that is a good thing for investors and markets. So the most recent rally we have seen in markets is at least partially rational, but we have yet to see what will happen when the US turns its attention to the EU.

What hasn't changed though is the impact that tariffs are going to have on the US economy and the economic slowdown that appears to be underway.

If the final US effective tariff rate ends at 10%, remember it was 2.5% at the start of 2025, this will be the highest and most protectionist we have seen the US since the early 1940's and with it remains the risk of high inflation with possibly slow economic growth (stagflation), which will bring concern for investors.

[1] Source: Bloomberg, 16.05.25
[2] A measure of how much of a tax a country's economy is bearing on its import
[3] A government-imposed ban on trading certain goods, services, or even all commerce with a specific country or group of countries

The short…

Market news

US-China trade deal agreed last weekend (11.05.25), brought about a powerful rally in global stock markets last week, with the US S&P 500, the largest US market index, recovering back to early January 2025 levels (in levels in US dollar terms). The deal itself reduces tariffs on both sides by 115%, bringing US tariffs to 30% and Chinese tariffs to 10%. A further 90-day pause period is now underway for a more substantive deal to be concluded but it has been well received by markets. We also so the US dollar rally and safe haven assets like gold, in general, fell back.

US-Saudi investment deal the US also appears to have secured an investment deal with Saudi Arabia and Qatar. It totals $1.2 trillion in value, involving a large investment by the Saudis in US military equipment, while also opening access to US artificial intelligence (AI) firms NVIDIA and AMD for Saudi's data centres. Unsurprisingly, all of the big US tech stocks got a boost from this and this led market gains mid-week. Separately, the US announced nearly a €25 billion in value deals with Qatar, including orders for US firm Boeing's aircraft.

US inflation, as measured by consumer price index (CPI), saw headline inflation reach 2.3% for April 2025. This was lower than feared and the third month in a row in which inflation fell. It may not be enough to convince the US Federal Reserve (Fed) to cut US interest rates any faster, however. In fact, a combination of pessimism about a recession and some fears that tariff driven inflation is yet to be reflected in data, have led markets to believe that there will only be two further cuts to rates this year from the Fund (similar to views about the European Central Bank). However, the University of Michigan Consumer sentiment survey's preliminary results for May have a very different read on inflation, with US consumers indicating they expect it to rise to 7.3% in the12-months ahead.

US dollar rebound in the early days of last week, in a response to the US-China trade deal and the lower US inflation figure we saw the US dollar rebound. The rise on Monday (12.05.25) was the strongest day for the currency in six months. However, much of this is likely to have been from hedge funds unwinding of trades in the currency and we are likely to see this recovery run out of steam. Adding to this were rumours that the US were making a weaker US dollar part of its negotiating stance with South Korea.

US 10-year yield[4] reached above 4.5% per annum on 14.05.25, a level not seen in almost three months (since 20.02.25).

President Trump's "One Big Beautiful Bill" has begun to make its way through the US Houses of Congress. This bill covers much of President Trump's proposed agenda including extending 2017 tax cuts permanently, amongst a range of other tax cuts, while also removing climate related incentives brought in under President Biden. One of the most controversial proposals is a reduction in eligibility for Medicaid, which supports access to medical services for the poorest Americans and could reduce health access for about 10 million people.

German Chancellor Merz used his inaugural address to the Berlin parliament to outline plans to transform the country's military into Europe's strongest conventional army to counter any potential threat from Russia. Germany's highest-ranking soldier indicated that the army needs to recruit 100,000 additional troops to bring the army to the level required.

UK economy grew by 0.7% in the first quarter, its strongest quarterly advance in a year and ahead of consensus expectations. However, most commentators are cautious as much of this was driven by exporters to the US ramping up production to get ahead of tariffs.

Moody's downgraded the US government's credit rating from AAA to AA1 on 16.05.25, citing concerns about the country's budget deficit and rising debt levels. The downgrade saw the US 30-year Treasury yield* rise over 5% per annum early Monday (19.05.25) morning.

[4] The income a bond generates over a period, often expressed as a percentage of the bond's value

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Table 1: 5 year historic performances

	2020	2021	2022	2023	2024
Global equities	6.7%	27.5%	-13.0%	18.1%	25.3%
US equities (S&P 500)	8.7%	38.2%	-13.0%	22.2%	33.6%
European equities (Stoxx 600)	-1.4%	25.8%	-9.9%	16.6%	9.6%
Emerging market equities	9.1%	4.9%	-14.9%	6.6%	15.4%
Global bonds	4.9%	-2.6%	-15.1%	4.5%	0.9%
US government bonds	8.3%	-2.0%	-12.5%	5.8%	0.3%
European government bonds	4.3%	-3.7%	-18.4%	7.2%	1.9%
Emerging market debt	-3.4%	6.4%	-9.8%	5.4%	15.1%
Broad commodities	-13.1%	37.0%	20.7%	-10.9%	7.0%
US corporate bonds	7.8%	-1.9%	-17.1%	5.8%	2.1%
European corporate bonds	2.4%	-1.2%	-14.0%	8.4%	4.6%

Source: Bloomberg 16.05.25. All returns expressed in euros.

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