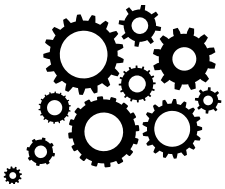


THINGS THAT MAKE YOU GO HMMM...

By Grant Williams

THERE CAN BE ONLY ~~ONE~~ TWO? (Part I)

Vol. 12 | Issue 12 | December 2025

"The aggressive use of sanctions may ultimately (and ironically) undermine their effectiveness by accelerating the development of alternative financial channels."

Janet Yellen, Former US Secretary of the Treasury

"Among these forces, one stands out as potentially transformative: the prospect of major oil producers moving away from dollar-denominated sales, ending the era of the petrodollar."

Diana Choyleva, Enodo Economics

"Strengthening energy trade cooperation with countries along the Belt and Road Initiative (BRI) initiative, particularly energy-rich nations, serves multiple strategic goals for China. It helps address China's growing oil consumption needs to sustain its economic development while reducing the economic challenges posed by its historically passive position in global oil trade... As China enhances its influence and pricing power in the global energy sector, it simultaneously promotes the use of the yuan in oil transactions, paving the way for the establishment of a Petroyuan circulation system. Over time, this shift has the potential to weaken the dominance of the US dollar and the European-led oil trade framework."

Bian Weihong, Director, Bank of China Research Institute

"China's relationship with Gulf states is currently at its best point in history. From an international political perspective, this is also the best period for China to strengthen economic and energy cooperation with Middle Eastern countries."

Niu Xinchun, Executive Director of the China Institute of Arab Countries

"If we can keep our competitors focused on us while we stay focused on the customer, ultimately we'll turn out all right."

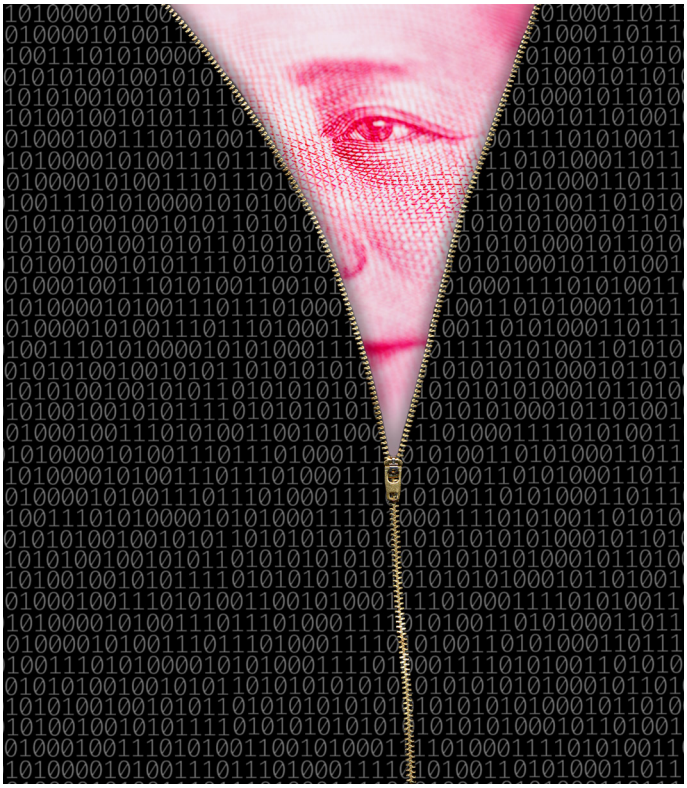
Jeff Bezos

p.04

p.32

THERE CAN BE ONLY ~~ONE~~ TWO? (PART I)

This is the first in a two-part piece to bookend the closing month of 2025 and the opening act of 2026, a year which may well end up being a memorable one—though possibly not for positive reasons. This piece was inspired by my recent podcast conversation with Diana Choyleva as well as my ongoing conversation with Luke Gromen in ***Shifts Happen*** *and my own writings*



There is a natural human inclination, when contemplating the possibility that the dollar might one day lose its pre-eminent position at the centre of the global financial system, to assume that it must happen with a certain dramatic inevitability.

We expect currency transitions to behave like revolutions, to arrive clothed in crisis, rupture and present themselves clearly as a moment when one world ends and another begins. Instinctively, we look for a collapse large enough to feel definitive, something that will one day be referenced as *the* turning point. However, even a cursory glance back through monetary history will demonstrate that history has always been, and remains, entirely unmoved by our narrative preferences.

This kind of change takes shape quietly, often unnoticed, until structures that once seemed permanent are proven to have thinned beyond repair.

None of the great monetary transitions of the past have arrived with banners flying, treaties signed or central bankers declaring a new age. Instead, they've unfolded through redirection rather than revolution, and through decisions made at the margins long before any public recognition followed. Behaviour changes first, narratives later, and by the time a new story becomes widely accepted, the system beneath it has already moved on.

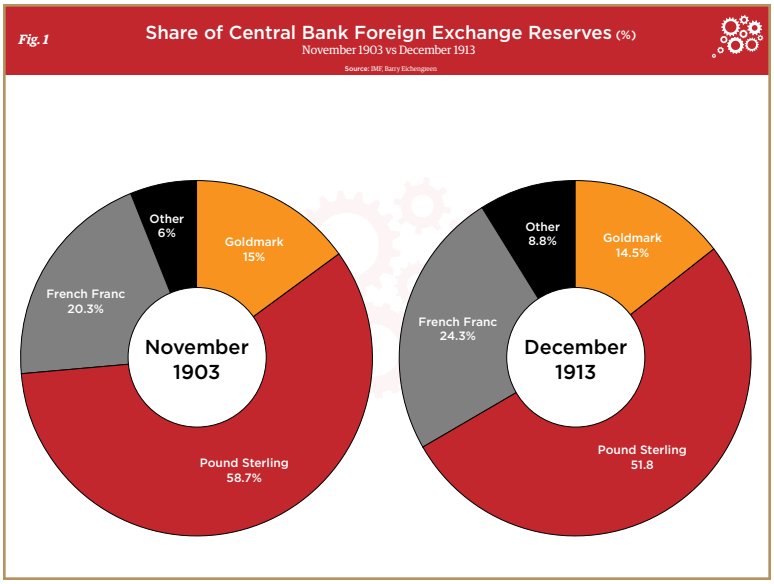
This is what makes the contemporary debate surrounding what's become known as *de-dollarisation* both so important and so misframed. It's commonly discussed as though it were a new arena of geopolitical confrontation, an emerging currency war in which China and the United States are destined to contest supremacy in some grand and visible struggle, with an eventual and obvious winner emerging. That framing feels intuitive to us because it borrows from familiar historical language.

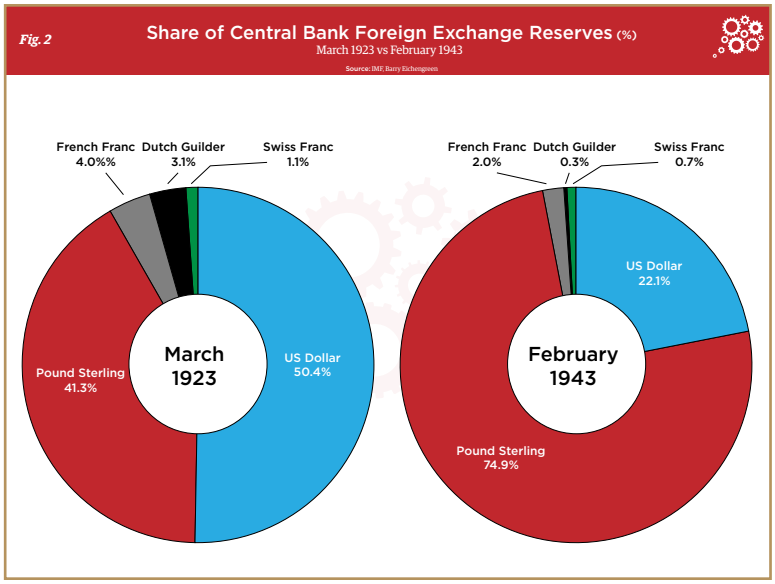
The Thucydides Trap, *The Great Power Competition*—however you want to frame it, the structure of the story is the same: great powers rise, great powers fall and a tense rivalry produces disruption and potential replacement.

However, the closer one looks at monetary history, the more inadequate this lens becomes. Reserve currencies are not dethroned in public and they don't fall because someone else declares ambition with sufficient confidence or volume. They lose their position when the world either discovers that it no longer needs them quite as much as it once did, or when the incumbent either overplays its hand, or stretches itself to the point where it no longer offers a viable path to repayment of the debts that build up in such a system.

At that point, we tend to wake up and find that something else, perhaps imperfect but useful enough, has quietly taken its place.

Take, for example, the rise of the US dollar.





If we go back to the 19th century, when Great Britain was, well, Great, the composition of Central Bank currency reserves reflected the tiny island nation's supremacy with almost 60% of Central Bank reserve assets held in pounds sterling (Fig. 1).

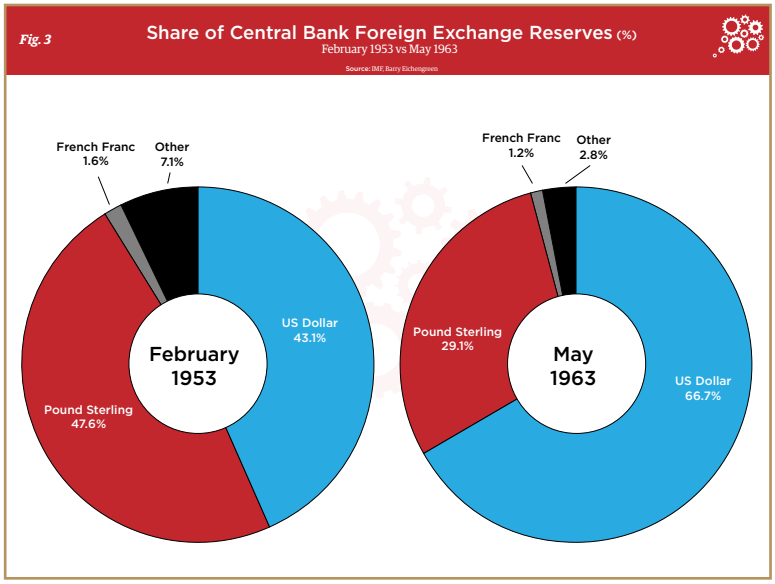
As you can see, by the eve of WWI, in December 1913 (the month the US Federal Reserve ~~crept into existence~~ was instituted), the pound's share of reserves had slipped a little, with the French franc gaining share but the US dollar was nowhere to be found.

Then came WWI and some interesting things happened.

With war raging in Europe, capital understandably fled to the safety provided by the United States—a literal ocean away from harm's way—dramatically reducing reserves held in sterling and all but eradicating those held in the currencies of mainland European nations (Fig. 2).

However, in the years that followed WWI, the British pound somehow managed to restore its supremacy, and, even in the depths of WWII, the pound accounted for almost three-quarters of global central bank currency reserves—a highly unlikely outcome in the mid-1920s.

It took The Bretton Woods Agreement in 1944 to cement the dollar's position at the centre of what was the first (and, to date, only, fully-negotiated) global monetary order. The change, while dramatic, was perhaps not as dramatic as you might think (Fig 3).



In 1953, the pound remained the world's pre-eminent reserve currency (albeit marginally), but the dollar's rise was now inexorable and, wherever the tipping point was on adoption, the world was now past it and allocation to the US dollar was accelerating dramatically.

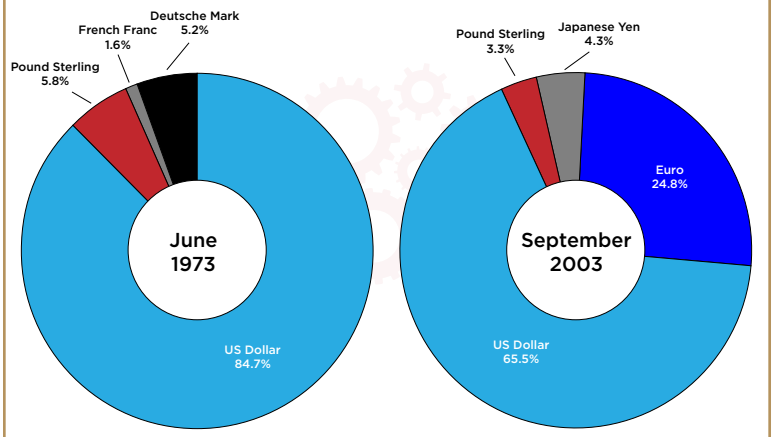
By 1963, the pound, while still constituting almost a third of global currency reserves, was well on its way to borderline irrelevancy, and the dollar was headed for the hegemony with which we are all familiar.

By 1974, with the signing of the petrodollar agreement, the US dollar was the undisputed king of the global monetary order, with a whopping 84.1% of global currency reserves held in US dollars (which is to say, US treasury bonds) (Fig. 4).

Fig. 4

Share of Central Bank Foreign Exchange Reserves (%)
June 1973 vs September 2003

Source: IMF, Barry Eichengreen

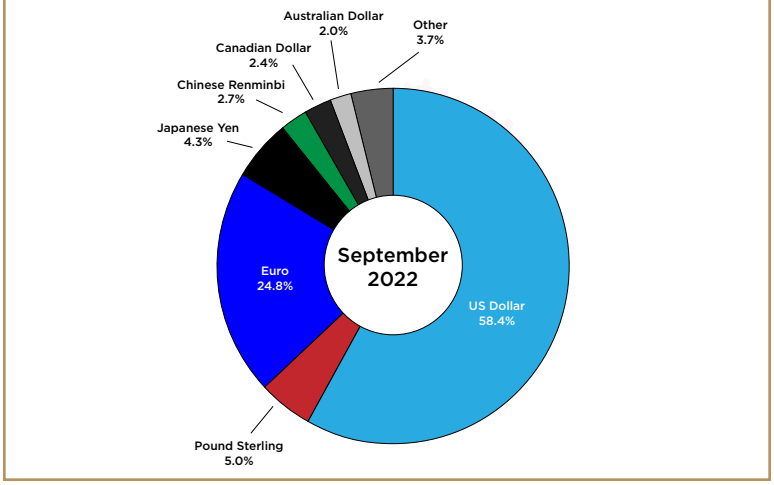


That, however, was the dollar's apogee, with the euro eating into its dominance after its establishment in 1999, and a broader mix evolving over time as globalisation led to the proliferation of multiple new cross-border trade relationships, many of which needed to find alternative ways to settle and, while the dollar-based SWIFT system still rules international trade settlement, the imperative was clear that alternatives were, if only at the margin, necessary (Fig. 5).

Fig. 5

Share of Central Bank Foreign Exchange Reserves (%)
September 2022

Source: IMF, Barry Eichengreen



But no matter how it got there, or the ebbs and flows of the dollar's rise to pre-eminence, it is and has been for decades the biggest, most important, most needed, most ubiquitous settlement and reserve currency on the planet.

Nothing else has come close.

However, the dollar didn't become the world's reserve currency because it was imposed by decree or demanded through diplomacy. It became central because it offered something the post-war world desperately needed and couldn't find elsewhere.

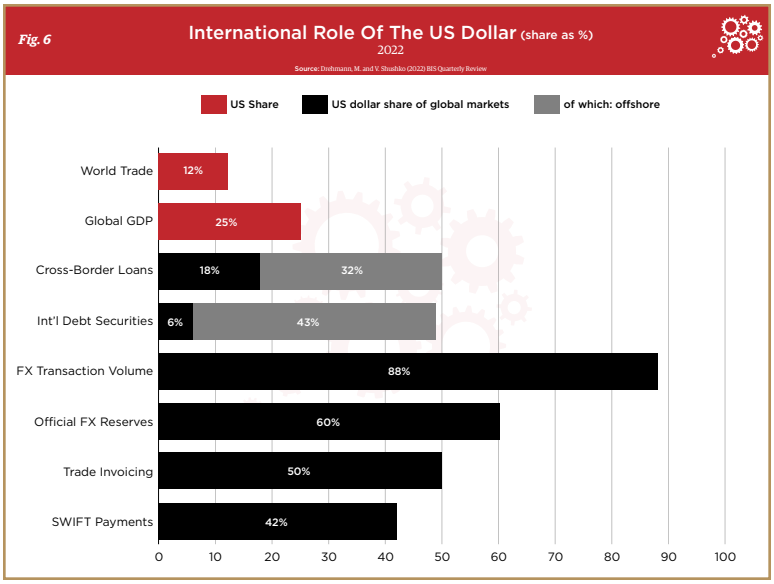
In the aftermath of WWII, vast swathes of the global economy were exhausted. Physical infrastructure had been destroyed, currencies had been destabilised, and capital was scarce. By contrast, the United States emerged from the war with a wholly intact industrial base, vast productive capacity and financial markets deep enough to absorb shifts in global capital without dislocation. Bretton Woods embedded the dollar in daily use. Contracts were written in it, trade was settled through it and capital was stored in it.

The architecture of the global monetary system that emerged after the war did much of the work itself. America offered something no other nation could match: a combination of liquidity, scale, legal framework and institutional stability that made the dollar not merely desirable, but avoidable to almost no one. In time, that usefulness hardened into habit, and habit into assumption. The dollar system was so stable and so omnipresent that its mechanics became invisible to those who relied on it. It simply existed, whether you liked it or not.

This invisibility, paradoxically, was the feature that allowed complacency to grow—not because the system failed, but because it succeeded so well that its continued functioning was taken for granted. Over the decades that followed, no comparable alternative was built, largely because no comparable alternative was *needed*. Capital markets elsewhere were shallower, legal systems less predictable and political risk, in may places, far, far greater.

What has shifted in recent years is not that the dollar has suddenly ceased to function. It continues to dominate international trade, global finance and reserve holdings (Fig. 6). Rather, what has changed is the world around it.

The architecture that underpinned American monetary leadership was designed for an era of slower financial flows, clearer ideological divides and more geographically tethered economies. It was built for a



world in which capital crossed borders less easily and information travelled less quickly and in which the central role of intermediaries was unquestioned and financial power was anchored to territory.

That world has vanished.

Modern commerce is a creature of speed and complexity. Supply chains now stretch across continents and capital moves instantaneously. In such an environment, the rigidities inherent in older structures such as correspondent banking, deferred settlement and comparatively glacial reconciliation, quickly begin to feel out of place. Yes, they still work, but no longer feel optimal and when systems stop feeling optimal, pressure for alternatives begins to grow.

New payment systems are adopted because they're faster, new settlement mechanisms are explored because they're cheaper and bilateral currency agreements begin to proliferate because they reduce risk in a fragile geopolitical environment. The world doesn't set out to rebel against a system; it simply finds ways to work around inconveniences placed in its way and, over time, those work-arounds accumulate into something more durable.

For years, this transpired largely out of public view, confined to central-bank seminars, infrastructure meetings and experimental pilot programmes. It was boring stuff, the kind only died-in-the-wool technocrats find a way to love. But, unfortunately for technocrats everywhere, history has a habit of dragging the mundane into the spotlight at precisely the moment when its significance can no longer be denied.

That moment arrived, somewhat quietly in March 2022, following the invasion of Ukraine.

When the United States and its allies froze the foreign-exchange reserves of the Russian central bank, the immediate reaction in the financial world was muted. The action was widely described as unprecedented, which it was, but novelty alone rarely makes history. What gave the event its global weight was not the scale of the freeze or even the identity of the target. It was what the action revealed about the nature of modern finance itself.

At the time, I wrote the following about the US Treasury's move to freeze Russian Central Bank reserves:

> ***(TEOTFWAWKI, TTMYGH, March 2022): ...the biggest wave made by the escalating Western sanctions against Putin's Russia was the move to sanction the country's central bank — a move that would have far-reaching consequences and, perhaps more than any other action, change the global financial system forever...***
>
> ***One country's 'bad incentives' is another country's 'national security concern'. What the West did by excommunicating Russia's central bank is fire a warning shot across the bow of every other central bank in the world, and it signals the end of an era.***
>
> ***By freezing Russia's FX reserves, the West essentially declared open season on anyone they may, at some point, deem a 'bad actor' and, while many will argue that they are never likely to merit that label, Russia has proven that's just not a chance you can afford to take...***

My prognosis at the time looks pretty good three years later:

> ***US dollar reserves are set to shrink as central banks diversify themselves away from an asset now weaponized in dramatic fashion.***
>
> ***This will mean a strong bid for gold from price-insensitive buyers in the form of those same central***

banks. It will also mean that new buyers have to be found for the mountain of US treasury issuance required to not only fund the US government's out-of-control** current **spending, but also to pay off the $168.5 trillion in entitlements due by 2050 as the Boomers continue to retire in their millions (that figure is courtesy of the US Debt Clock and was correct at time of writing but is guaranteed to be low at time of reading).

This will put pressure on the dollar which will, in turn, drive commodity prices higher, demanding higher interest rates if the ~~transitory~~ entrenched inflation is to be tamed.

Yes, inflation has supposedly moderated, but the dollar is under significant pressure and gold has found a solid bid from central banks and, increasingly, the investment community.

But the deeper change unleashed by the freezing of those Russian central bank assets was significant.

For the first time since the modern reserve system had been assembled, a major central bank discovered that its reserves were not simply financial instruments subject to market fluctuations, but political assets vulnerable to external control. What had long been assumed to be a country's ultimate insurance policy against crisis—access to its own reserve assets—was revealed to be conditional on the 'correct' political alignment.

That realisation travelled faster than any headline ever could. What central bankers absorbed in days would once have taken years (and innumerable seminars) to dawn on them. Reserves were no longer to be understood merely in terms of interest-rate exposure and currency mismatch, but in terms of sovereignty risk. The distinction, long treated as theoretical, became immediate and practical.

For decades, reserve management had been framed as a technical discipline insulated from geopolitics, possessed of it sown language, its own models and its own culture, with 'risk' merely something to be hedged through diversification and yield optimisation. Moreover, political instability was discussed in the abstract, but rarely treated as something that could directly affect access to assets held in the reserve portfolio. Central banks prided themselves on neutrality and, whether that pride was ever fully justified, matters far less today than the undeniable fact that it shaped behaviour.

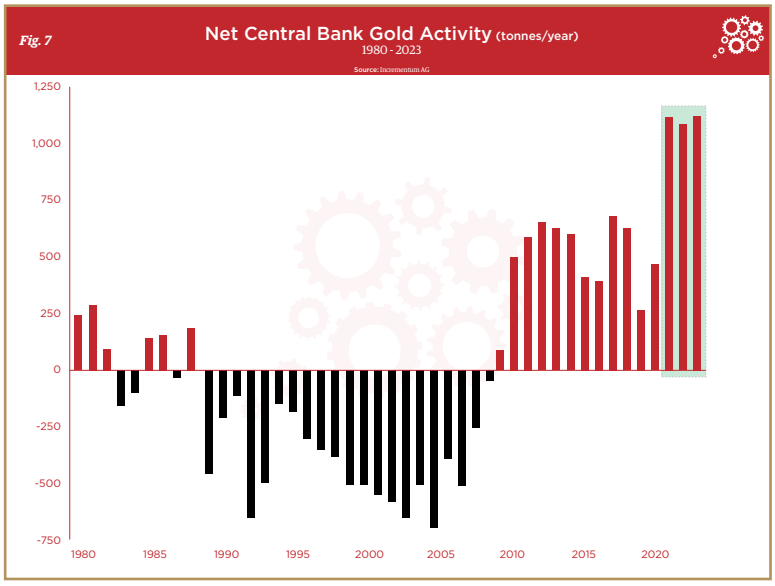
The freezing of Russian reserves shattered that perception in a single act. It demonstrated that the system, however sophisticated, was not neutral infrastructure, but rather policed space. It contradicted decades of unspoken assumption that central bank money sat above political conflict and, in that instant, reserves became visibly and overtly political capital.

That, Dear Reader, is *everything*.

There was no dramatic exodus from the dollar that followed. No mass divestment, no public rebuke, no currency crisis triggered by political anxiety.

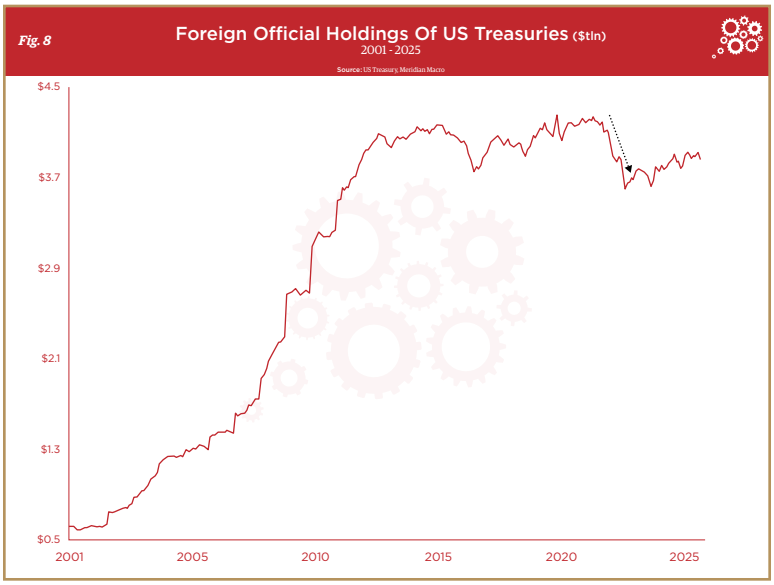
Yet the impact of that single, politically-motivated action was profound. The conceptual framework used to understand reserve assets changed instantly, and when frameworks change, behaviour always follows—even if it does so quietly.

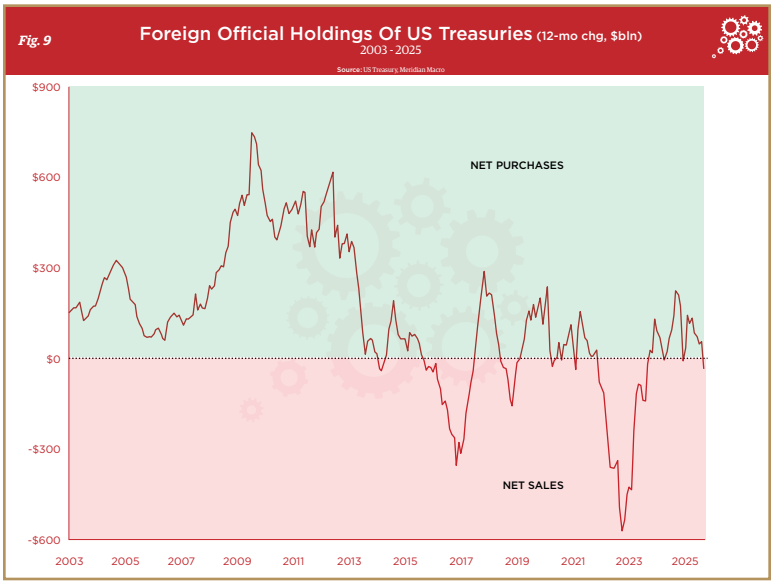
In the months that followed, central-bank balance sheets began to tell a more revealing story than any statement ever could. Official purchases of gold accelerated to levels not seen for a generation (Fig. 7) and, while some of that could be explained through inflation concerns or routine diversification, the sheer scale and persistence of buying pointed to something much deeper, much more profound. Gold wasn't being accumulated because it offered yield, but because it offered independence and security.



Unlike sovereign bonds, gold bears no counterparty risk. It exists outside the digital permissions structure that governs modern finance. Assuming it is secured under a given country's own auspices, it can't be frozen, defaulted upon or rendered inaccessible by administrative decree. It's economically awkward, politically inert and operationally unfashionable, which is *precisely* what made it instantly relevant again.

At the same time, holdings of US Treasuries began to flatten in certain jurisdictions and decline in others (Fig. 8 & 9). This wasn't so much a judgement on American monetary policy, nor a sudden loss of faith in the Federal Reserve but, rather, hedging in its purest form. The moment the structural assumption of political sanctity on sovereign reserves ~~fell~~ was swept away, portfolios *needed* to be adjusted. It wasn't a matter of choice.





It would be wrong to interpret these moves as rebellion or protest. Buying gold and quietly offloading treasuries at the margin simply offered an insurance policy, purchased quietly and incrementally, with the objective not the dismantling of the existing system, but a reduction of dependence upon it.

That single decision by the US Treasury didn't destroy the dollar's role, but it did alter its psychological character, and the timing of that alteration was crucial. What had once been understood as neutral infrastructure was now visible as politically governed system and, once that recognition sets in, the relationship between user and custodian inevitably shifts. Crucially, throughout the period of US dollar hegemony, there was no real competition—or, more accurately, no real competitor. But now a rival was waiting in the wings in the shape of a rising China.

History suggests that confidence rarely collapses neatly. It thins, adjusts, and moves sideways before it moves away and, in the case of global reserve systems, they don't disappear overnight. Instead, they get diluted gradually through a series of marginal decisions—and the occasional catastrophic misstep.

To understand the shape that path eventually takes, we needn't speculate. History provides a useful template, beginning in the Summer of 1956.

If the freezing of Russian reserves in 2022 forced the present generation of central bankers to confront a truth they'd long preferred not to examine, then the 1956 Suez Crisis serves as the historical analogue that explains why such moments resonate far beyond their immediate circumstances.

Suez is remembered popularly as an episode of imperial hubris, a late and clumsy attempt by Britain and France to impose authority in a post-colonial Middle East. But it's far more useful to understand it as a monetary event disguised as a geopolitical one, the final revelation of something that the world already knew to be true—that Great Britain no longer remained financially sovereign.

For more than a century before Suez, sterling had been the connective tissue of global commerce, with

London not simply a marketplace, but the mechanism through which the world's trade, credit, and insurance were conducted. The British Empire, at its height, was not only territorial but financial; it ruled shipping lanes and capital markets with equal assurance, and the pound reflected that reach in its function as a medium of exchange, a store of value, and a unit of account on multiple continents. Confidence in sterling didn't arise from patriotic sentiment, but rather from the City of London's institutional strength, predictable law, deep markets, and an aura of continuity so established that it eventually became invisible to those who benefited from it.

Sound familiar? Thought it might.

Beneath the surface, however, two world wars had altered the mathematics of Britain's dominance far more than the status quo suggested.

Britain emerged from WWII no longer the world's banker but as its debtor-in-chief, burdened by loans, dependent on American support, and presiding over an industrial base that no longer led the world it had once supplied.

Sound familiar? Uh huh...let's continue...

Reserve systems rarely respond to a hegemon's weakened fundamentals in real time. Instead, they take their sweet time, sustained by confidence and familiarity long after confidence has become more hope than reality.

The Suez Crisis brought that misalignment into sudden and unforgiving focus.

When Egyptian president Gamal Abdel Nasser nationalised the Suez Canal in 1956, London and Paris interpreted the act in political terms and responded militarily, convinced that this was a challenge to their elevated standing in the world order that could only be restored through force. What they misjudged was not the tactical complexity of the operation, but the dimension in which it would be decided. The crisis was not settled in Egypt. It was settled in financial markets.

The United States, concerned less with the canal than with the stability of the post-war order (oh-so-close to the centre of which it happily sat). Sensing a moment which would allow it to improve its own position by weakening that of its 'allies', it reneged on the 'special relationship' it had with Great Britain, making plain that it wouldn't provide financial support to sustain an imperial enterprise it no longer endorsed.

Like the Russians in 2022, all four countries involved in the Suez Crisis (Great Britain, France, Egypt and Israel) discovered almost immediately what that decision meant in practice.

Here, courtesy of the IMF, is a potted history of the crisis for those among you unfamiliar with what is a chronically under-appreciated event in global monetary history:

> ***(IMF): On July 26, 1956, Egypt nationalized the Suez Canal Company and unilaterally assumed control of the canal from the international consortium that had run it for nearly a century. France, Israel, and the United Kingdom almost immediately began planning a joint military action to retake control, while they sought to win international support for a diplomatic solution. When diplomacy failed, Israel invaded the Sinai on October 29, and France and Britain used Egypt's counterattack as an excuse to attack Egypt by air from the Mediterranean two days later. The fighting shut down the canal, which was the major shipping channel between Europe and Asia and a vital link in the transport of petroleum from the Middle East. One week later, however, Britain undercut the operation by accepting a United Nations resolution for a ceasefire. On December 3, the British government announced that it would withdraw its troops over the next few weeks. France and Israel soon also withdrew, and Egypt reopened the canal under its own control the following April.***

That's what *happened*. Here's why it *mattered*:

> ***(IMF): That this brief flare-up is universally regarded as a crisis is primarily because of the upheavals it engendered in political relations. It successfully climaxed Egypt's longstanding campaign for full independence from European dominance. It demonstrated Israel's ability to defend and expand its borders militarily and thus to survive as a nation. It weakened France just as the Algerian war was intensifying. It exposed a rift in relations between Britain and the United States***

over post-colonial policies at a time when both wanted to counter the rising regional influence of the Soviet Union. In Britain, it brought a sad end to the brief ministry of Anthony Eden and ironically elevated Harold Macmillan in his place. In view of the central place of Suez in the mythology of the British Empire—Eden had once called it "our back door to the East," and generations had grown up on Kipling's evocation of an uninhibited life "some-wheres east of Suez"—the loss of control over the canal was devastating for those with lingering Victorian aspirations. In the Middle East, it solidified Gamal Abdel Nasser's budding leadership role and hinted—if only temporarily—at the possibilities for Arab unity. A vast and still-growing literature has analyzed each of these facets in exquisite detail.

But beyond the politics of the Suez Crisis, lay the more important, more lasting damage.

Interestingly, the IMF's assessment of the economic damage done by the crisis was fairly benign:

(IMF): The economic consequences of Suez were more subtle and temporary and would not by themselves have constituted an international crisis. Notwithstanding the crucial importance of the canal for certain trade flows, the economic impact of its closing was limited by its short duration. By October, Egypt had already proved that it could run the canal safely and efficiently without European assistance. For the six months that the canal was closed, the resulting cost increases, delivery delays, and trade diversion weakened the current account positions of all four of the combatants, but normalcy was largely restored within another six months.

No biggie, right?

Wrong.

Egypt, Israel and France each went, cap-in-hand to the IMF, and were granted loans to help them through the turbulence created by Nasser's actions.

Great Britain, her stiff upper lip firmly set, soldiered bravely on until she too was forced to seek help and the events of 1956/7 when viewed exclusively from the British perspective are vital to understand.

In the summer of 1956, Britain had entered the Suez drama from a very different position to France, Israel and Egypt. On the surface, its external accounts looked sound. While France and Israel were watching their current-account positions deteriorate sharply and Egypt faced the loss of canal revenues, the United Kingdom was running a respectable surplus: £159 million in the first half of the year, rising to a total of £245 million for 1956, with a similar outcome in 1957.

However, the problem lay not in the trade numbers, but in the psychology of markets that watched sterling as a reserve currency with a published reserve floor of $2 billion and a fixed parity of $2.80 to the US dollar that the authorities believed they must defend. Once Suez erupted, the question became not whether Britain could pay its way, but whether it could hold that rate without external help.

For British policymakers, the $2.80 parity, set in 1949, had acquired totemic significance. It was deemed appropriate for trade, and crucial at a moment when the closure of the canal threatened to force the UK to pay 'expensive dollars' for diverted oil imports.

More profoundly, maintaining parity was seen as essential to preserving the pound's wider role as a reserve currency. A problem for Great Britain, an opportunity for the United States.

Although sterling was not yet fully convertible post-WWII, capital controls were patchy, and the currency was widely held abroad, making it uniquely vulnerable to speculative pressure in a way Egypt's or Israel's currencies were not. Falling through the self-imposed reserve floor, clearly visible in the monthly figures, would be read in markets as a signal that devaluation or floating could no longer be avoided. In that context, the Suez Crisis didn't merely threaten British foreign policy, it threatened the credibility of Britain's money.

Harold Macmillan at the Treasury and Cameron Cobbold at the Bank of England were united in seeing any devaluation as catastrophic. They regarded a second devaluation, a mere seven years after that of 1949, as something that would risk breaking up the sterling area, undermine the nascent European Payments Union, shrink trade and unleash domestic inflation. In Cobbold's words, it was a *"disaster to be fought with every weapon at our disposal."*

Macmillan agreed.

Both understood that the $2.80 rate could not be held without American support, and that such support was unlikely while Britain was defying Washington over Egypt, yet they still refused to contemplate either devaluation or a float. In effect, they made defence of the parity non-negotiable, even as they launched a military operation that placed sterling under maximum strain.

When Nasser nationalised the canal on 26 July 1956, the Bank of England had already prepared for trouble with plans to block Egyptian accounts. When selling pressure on sterling materialised, officials initially assumed that Egypt was dumping its holdings, and they responded by freezing transfers between sterling and the Egyptian pound. But this gesture did nothing to stem the broader speculative pressures.

Over the next four months reserves declined steadily toward the $2 billion floor, temporarily held above it only by a lucky inflow of $177 million in September from the sale of the Trinidad Oil Company to, of course, an opportunistic American buyer.

The Bank's first line of defence was direct intervention in the foreign-exchange market, buying sterling against dollars, while dismissing the classic response of raising interest rates as ineffective in a crisis of confidence. But, when a central bank is forced to intervene directly in FX markets, all participants know the game is up. It's just a matter of time.

Behind the scenes, Macmillan was seeking a second line of defence. Confident in the 'special relationship,' between Great Britain and the United States, and bolstered by his own personal ties to the US, he ~~assumed~~ hoped Washington would step in to support sterling by waiving interest on wartime lend-lease debts or providing fresh loans through the Export-Import Bank. Failing that, he fully expected that the IMF would provide substantial support, both because Britain had the second-largest quota and because it held a supposedly unique importance as a founding member.

The IMF and World Bank Annual Meetings in Washington at the end of September offered the obvious moment to test the waters.

Macmillan, attending as Britain's Governor, met US Treasury Secretary George Humphrey, Secretary of State John Foster Dulles and President Eisenhower, came away with the impression that some form of US financial support would be forthcoming after the November presidential election. He returned to London convinced that his American counterparts would not leave sterling undefended.

Hmmm...

Through October, as the Bank continued to run down its reserves and the Cabinet prepared for war with Egypt alongside France and Israel, Macmillan took no further decisive steps. When Israel invaded Sinai on 29 October and Anglo-French bombing began two days later, US and international opposition hardened, and the drain on British reserves accelerated into a genuine speculative attack. On 2 November, the UN General Assembly passed a US-sponsored resolution calling for a ceasefire; within days the pressure became intolerable.

By early November, it had become clear that financial forces were driving British policy, forcing capitulation. The Cabinet agreed to a ceasefire on 6 November under intense diplomatic and market pressure, and Macmillan later conceded that the US refused to support Britain's request to draw on the IMF until London had accepted a ceasefire and, in practice, full compliance with the UN resolution, including withdrawal of troops.

L to R: Dulles, Eisenhower, Humphrey, Cobbold, Nasser, MacMillan

Once that political condition was met, attention returned to assembling a package large enough to convince markets

that sterling could withstand attack. Cobbold resisted approaching the IMF immediately, fearing that it would signal weakness unless part of a broader support arrangement, while officials in the Treasury suspected the Fund was their only real hope. Both agreed that if they went to the IMF they should seek the maximum possible credit, up to three tranches, or 75% of Britain's quota, a sum unprecedented for a major country.

Britain's weakness had been exposed, the US realised it had the upper hand and like any good ally, it stepped on Great Britain's neck.

Through November, technical consultations with IMF staff in London continued at a routine level, but the real decisions were being taken in Washington. Per Jacobsson, the incoming Managing Director, was persuaded during a stop in London that Britain's exchange rate was 'fundamentally sound' and that a major package was justified to defend sterling and protect the wider system. On taking office in early December, he resolved that the UK should receive a total of around $1.3 billion. At the same moment, Humphrey was wrestling with the fear that a large IMF operation for Britain could trigger either a run on the Fund or higher US interest rates, but eventually reversed himself, concluding that the best way to restore confidence was to go big: Britain would draw half its quota immediately and secure a stand-by for the rest.

On 3 December, with British reserves about to fall below the symbolic $2 billion floor, London finally had its answer. The United States signalled support for a large IMF operation, on condition that Britain conformed to the UN line, and the Fund's Executive Board approved a drawing of $561 million with an additional $739 million available on stand-by.

Macmillan was able to go to the House of Commons on 4 December, announce the heavy loss of reserves in November, and simultaneously unveil a rescue package designed to 'fortify' sterling. The very fact that the IMF and the United States were now standing visibly behind the pound was enough to halt the immediate run. Reserves stabilised above the floor and, although Britain later renewed the stand-by in 1957 as policy doubts resurfaced, it never had to draw the remaining funds. The episode demonstrated, more clearly than any speech could have done, that British power in 1956 depended less on tanks at Suez than on credit in Washington.

The events surrounding the Suez Crisis were hugely important because they demonstrated how, at the appropriate moment, even the world's hegemonic currency can be toppled when ambition collides with opportunity.

Britain, while still a major power, was economically fragile in 1956 and, in the end, that fragility was exploited by the US to usurp Britain's place at the top of the global monetary order.

The United States manufactured the moment in which the world understood Britain could no longer guarantee its own currency without external patronage. From that point onward, sterling's authority rested not on its own credibility, but on borrowed confidence.

Nothing in the visible world had broken. Markets opened, trade continued and London remained busy. Yet beneath that continuity, something decisive had occurred. Central banks and international institutions did not record the end of sterling's reserve status on that day. But they began, quietly and pragmatically, to act as though it had.

Confidence didn't collapse, it simply reorientated itself in real-time.

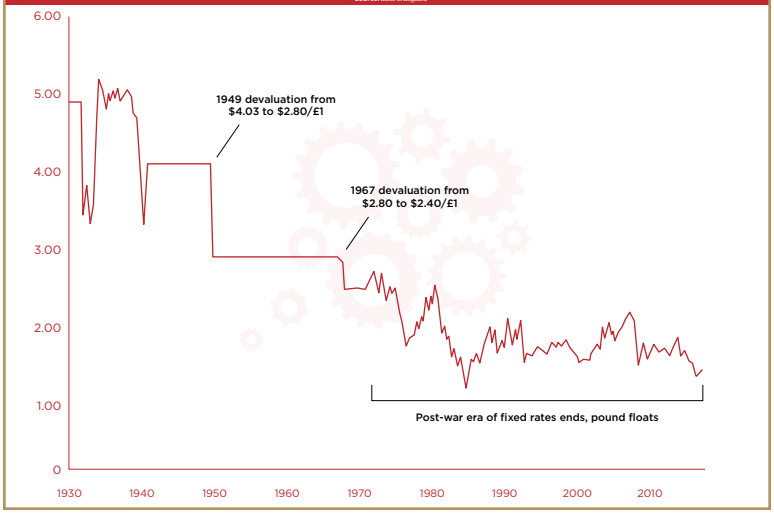
Reserve managers trimmed exposure, contracts were increasingly denominated elsewhere and the dollar expanded into roles the pound had once filled.

Suez, in this sense, should be read less as an episode of diplomatic miscalculation and more as a stress test that Britain failed. The British Empire didn't fall because it lost a canal, it fell because it lost financial independence, and with it the ability to convert ambition into action without asking for permission from its 'friends' in Washington.

In the decades that followed, Britain suffered through wage restraint, repeated devaluations (Fig. 10), balance-of-payments crises, and recourse to international lenders whose involvement would once have been unthinkable. The privileges that came with issuing the world's reserve currency—the capacity to borrow without consequence, to finance conflict without currency risk and to absorb capital without

Fig. 10

British Pound vs US Dollar
1930 - 2015
Source: Bank of England



distortion—had quietly disappeared. Britain didn't become poorer overnight, but it became constrained, and that was the death knell for sterling as the backbone of the global monetary system.

The lesson embedded in Suez is not simply that currencies can die when politics goes wrong, but also that monetary authority collapses the moment capital decides it's no longer safe to rely upon it.

This is what makes Suez so uncomfortably relevant to the present.

Suez didn't kill sterling, it merely removed the ability for its trading partners to wilfully ignore its frailty.

Sound (potentially) familiar? On we go...

Suez quietly marked the moment at which the architecture of a new system completed its consolidation. The groundwork had been laid long before British ambitions collided with mathematics in the Eastern Mediterranean. Bretton Woods, designed in the closing years of war, had already mapped the contours of a world in which American capital and American institutions would form the structural spine of global finance. Suez simply made clear that the transition had already occurred in substance if not yet in symbolism.

What distinguished the American rise from every reserve-currency episode that preceded it was not merely scale, but timing. The United States became the world's monetary anchor at the precise moment the world was rebuilding itself. Capital scarcity in Europe and Asia created infinite demand for liquidity, while destroyed infrastructure guaranteed demand for investment. America alone possessed reserves, industrial capacity, and institutional coherence at sufficient scale to fulfil those needs simultaneously.

In earlier centuries, reserve currencies grew alongside empire, secured, for the most part, by maritime dominance and reinforced through colonial trade networks. The dollar rose through reconstruction, international lending, and market architecture rather than conquest. In funding Europe through the Marshall Plan, the United States exported both money and confidence, embedding its legal norms, economic assumptions and commercial standards into the rebuilding of an entire continent. As they circulated, dollars became the foundation of recovery itself.

By establishing a global standard anchored to convertibility into gold and discipline (at least in theory), Bretton Woods offered the world a financial lubricant that *appeared* neutral, even as it was deeply American in design.

Ultimately, it was, and remains, nothing of the sort.

Currencies remained nominally sovereign, but they orbited a system whose centre of gravity lay unmistakably in Washington and New York. For a world exhausted by inflation, disorder and war, stability was not merely welcome, it was intoxicating.

Yet the greatest achievement of the post-war system was not its architecture but its psychology. It didn't require enforcement to persist because it operated through the complete acceptance of its members.

Nations held dollars because they worked, transacted in dollars because so many others did (in large part, thank to the 1974 petrodollar agreement), and invested in America because American markets offered depth and continuity unavailable elsewhere. No other country could combine rule of law, entrepreneurial capital, and political continuity with such credibility at scale.

Global trade spoke the language of the dollar *not* because it was demanded, but because it was ubiquitous and this ubiquity proved far more durable than any treaty.

But it was precisely that ubiquity, rather than any dollar dominance, which turned what began as a preference into complete dependence.

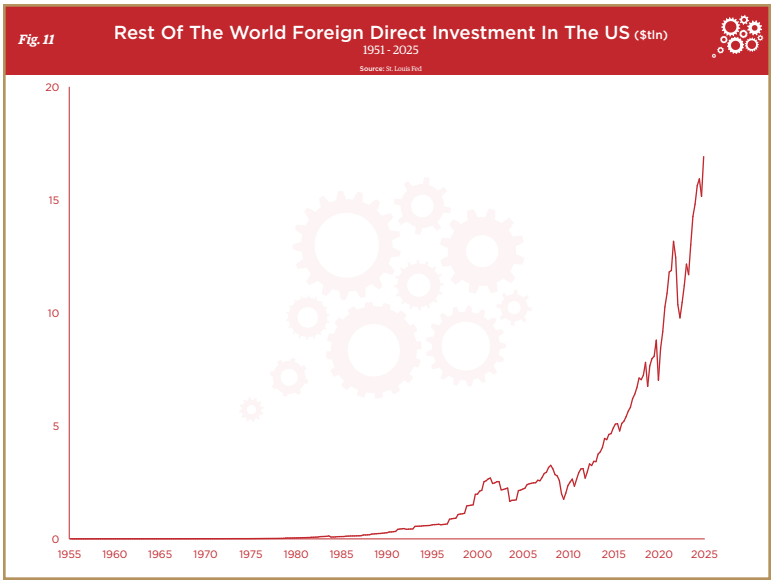
Systems that function well for long periods breed confidence, and confidence eventually becomes a toxic mixture of complacency and entitlement. For decades after Bretton Woods, America benefited not just from issuing the world's money, but from writing the conditions under which money itself was defined. Legal frameworks, accounting rules, capital requirements and compliance standards flowed outward from the United States alongside dollars. Finance, in effect, converged around mostly American assumptions.

But convergence carries its own risks.

When all liquidity passes through the same pipes, the failure of any segment becomes systemic by definition, and when regulation and settlement are concentrated under one jurisdiction, political risk and financial risk cease to be distinct.

Over time, this concentration would prove to be perhaps the dollar-based financial system's greatest strength...however, with the actions of March 2022, it has proven to be potentially its greatest vulnerability.

For decades the system worked remarkably well. Inflation, once banished, appeared vanquished, and capital surpluses flowed obediently into American assets (Fig. 11), allowing the United States to consume far more than it produced without visible strain.



Financial innovation multiplied, credit expanded and the American consumer became the global engine of demand and the global absorber of surplus.

And, for as long as the system held, it delivered extraordinary results.

There was, however, a subtle inversion taking place beneath the surface.

The dollar's role as the world's most important ~~money~~ currency gradually and, imperceptibly altered the incentives that once sustained it. As easy financing muted fiscal discipline and capital inflows distorted domestic asset prices, Wall Street grew ever larger, ever more elaborate, and increasingly detached from the real economy beneath it.

Meanwhile the industrial heart of the United States thinned as production moved offshore in pursuit of lower costs, migrating to the very nations whose surpluses would ultimately return to American capital markets as lending.

For decades, 'globalisation,' as this wave became known, looked for all the world like it brought nothing but benefit, and yet, beneath its surface, the tide carried consequences that no one either expected, or expected to matter.

Democracies tend to adapt poorly to distortions created at a macro level. Over time, credit expands faster than productivity, consumption faster than output and, as a result, debt faster than discipline.

Each generation not only inherits the system as it *exists*, not as it was built, but forgets the assumptions that once made it reliable and drifts farther away from its intended purpose as a new generation of politicians promises and spends—abusing the exorbitant privilege bestowed upon the issuer of the world's reserve currency at any (and, sadly, every) point in time.

The system endured nonetheless, absorbing shocks with impressive resilience. Oil crises, currency panics, and financial busts came and went. Latin American crises flushed through Wall Street and cleared. The Asian financial contagion of the late 1990s tested liquidity, but reinforced rather than weakened America's centrality. Even the Global Financial Crisis failed to unseat the dollar, in part because the only

asset considered safe at a time when toxic American credit threatened the system's stability was the currency in which the vast majority of that debt was denominated.

Go figure.

What that episode truly demonstrated was not merely the inertia of dollar dominance, but the degree to which the rest of the world would tolerate imbalance rather than experiment with alternatives. Countries whose reserves had been annihilated through the crisis nonetheless returned to the system they already knew.

Better the devil you know.

And yet, even though it's never immediately obvious, each crisis subtly changes what participants are willing to accept next time around. This is one of the great paradoxes of monetary history. The longer a system survives, the more fragile its assumptions become.

At no point did the American system appear to display visible weakness. What it did instead was evolve into something too large, too interconnected, and too essential to fail easily or, importantly, change quickly.

This is why the emergence of possible alternatives over the last decade didn't resemble any kind of revolt.

The BRICS ~~seemed~~ are disorganised and, some believe, innocuous, but they hijacked the debate and hardened the position taken by both sides: either the dollar is dead, or the BRICS are a nothingburger.

There's nothing in-between. Or so it would seem...

Meanwhile, in the background, China began constructing its own payment infrastructure as protection against the dollar's increasing weaponization—not as a challenge to its hegemony. Energy exporters sought currency diversity as insurance and smaller nations built settlement options not as retaliation, but as both resilience and redundancy. None of this required coordination because it emerged naturally thanks to shared interests, and beneath it all sat the reality that the system, while formidable, had begun to show its age.

If Britain lost reserve leadership when it could no longer defend sterling alone, America now faces a far subtler dilemma. Its system remains dominant, but dominance is no longer exclusive. For the first time since Bretton Woods, the world is building *around* the dollar rather than simply through it.

Importantly, the nature of that dominance *isn't* Bretton Woods alone, nor even American industrial might, but the evolution of a system that turned trade imbalances into financial fuel.

The world didn't merely adopt the dollar as a medium of exchange. Through the petrodollar agreement, it accepted, largely without debate, an arrangement in which the accumulation of surplus in one part of the globe automatically financed consumption in another. In this circular flow of capital lay the true engine of American influence, an influence rarely described accurately because its workings were neither ideological nor explicit.

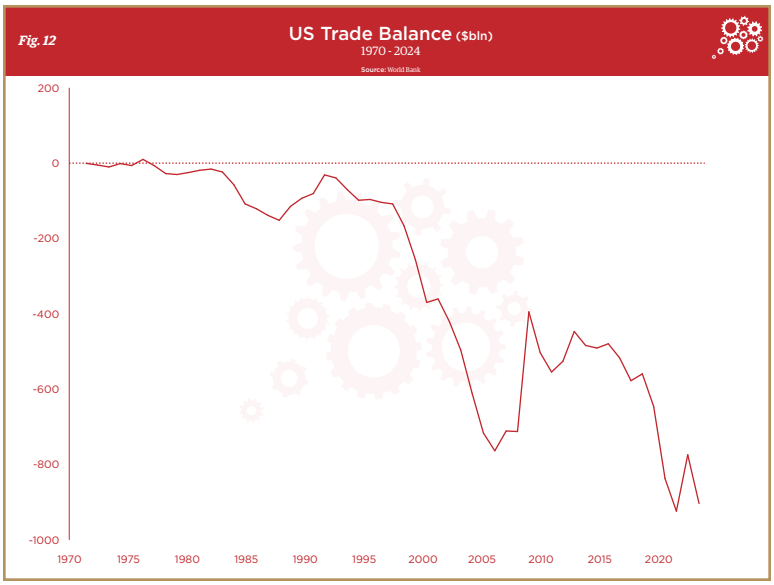
Nowhere was this more evident than in energy markets, which, of course, sit at the base of modern economic life. Oil pricing in dollars was possibly not initially conceived as a grand instrument of empire, but likely more as a convenience that simplified trade among producers and consumers scattered across continents. Over time, however, petrodollars didn't simply exist as accounting entries on contracts; they accumulated, and then, crucially, returned home in the form of treasury purchases.

Energy exporters found themselves awash in dollars, as an operational outcome. With limited domestic capacity to absorb that inflow in a productive way, those surpluses sought a home, and American capital markets offered a refuge that no other destination could match at scale. Thus was born the great recycling mechanism that underpinned late-twentieth-century American prosperity: oil revenues flowed outward, and financial claims flowed back in.

This system achieved something few trade structures ever manage. It harmonised the interests of producer and consumer through inertia rather than negotiation. Energy exporters enjoyed largely stable dollar revenues, the United States financed ~~excessive wanton~~ consumption through foreign savings, and global imbalances, rather than causing breakdown, fuelled continuity.

It's difficult to overstate how extraordinary this arrangement proved to be in practice. For decades, America lived with persistent trade deficits that in any other historical context would have provoked some kind of a crisis (Fig. 12). Yet remarkably, these imbalances were not merely tolerated by foreign governments, they were actively financed by them. The very nations exporting goods and energy to the United States reinvested their earnings into American debt, equities and assets, completing a financial circuit that rewarded all participants in the short term while quietly altering the structural incentives of the system.

Fig. 12



The effects were visible but poorly understood.

Consumption expanded, asset markets rose, and borrowing costs fell. Meanwhile, American policymakers grew accustomed to deficit financing without penalty, and American consumers learned to expect ever-cheaper abundance unconstrained by production.

What went ~~unnoticed~~ ignored for far too long was that this system didn't merely reflect American strength. It actively reshaped it.

Easy financing dulled fiscal restraint and persistent capital inflows inflated financial assets faster than wages as the country's manufacturing base was offshored. Meanwhile, finance expanded *inward* and political promises became easier to make because the hard choices associated with funding them were always deferred to the future.

The world didn't conspire to perpetuate the dollar system. It allowed it to continue to exist because it functioned, and because in the early decades it had delivered growth that felt universal enough to be defensible. The post-war boom, fuelled by reconstruction and consumption alike, created an atmosphere in which debt appeared benign and trade imbalances seemed harmless. As long as everyone was growing, no one wished to examine the machinery too closely.

By the turn of the new millennium, however, the fragilities had begun to emerge. Asset prices disconnected from income as credit expanded completely out of step with productivity and financial complexity accelerated at breakneck speed.

Incredibly, the Global Financial Crisis didn't break this arrangement, despite its epicentre being squarely in the United States. If anything, it reinforced it.

In the midst of chaos, capital fled not *away* from the dollar but toward it, teaching governments across the world that, while American finance had grown dangerous, it remained indispensable and, when the system convulsed, it was American liquidity, supplied in abundance by the Federal Reserve, that stabilised it.

What the emergency programmes of 2008 and beyond truly demonstrated was not merely the necessity of central intervention, but the extent to which the system had come to rely upon it, and with each successive rescue, the line between extraordinary and routine intervention grew thinner.

What began to shift in the decade following the financial crisis was, unfortunately, not policy.

Advances in technology, payments infrastructure, and bilateral agreements introduced something new into the system: choice.

China's trade expansion, the Gulf's capital diversification, and the gradual multiplication of settlement routes all began to exert pressure. When capital has *other* places to go, it doesn't need to flee to express dissatisfaction, it simply drifts away into a friendlier embrace.

This is the subtle danger for any reserve system. It won't lose control through mutiny, but rather through

increasing obsolescence at the margin.

The petrodollar agreement contains within it precisely this vulnerability. It isn't the pricing of oil in dollars that matters, it's the recycling of proceeds into American markets and it's *this* dynamic which constitutes the vital part of the entire edifice.

The moment financial gravity shifts is not when pricing systems change, but when *investment behaviour* does. Capital cares less what unit of account is printed on a commodity contract than where the resulting surplus finds its home and *this* is what's now changing beneath the surface of global markets.

Gulf sovereign wealth funds are allocating more capital eastward—not for political reasons, but because growth and demand have shifted in that direction over time. China is no longer simply a buyer of energy and commodities, but increasingly a long-term commercial and financial counterparty. Investment that once concentrated naturally in the United States is now spread more broadly across Asia and the Middle East, where infrastructure development, manufacturing capacity, and technology adoption are expanding at a much faster pace.

In my recent podcast discussion with Diana Choyleva of Enodo Economics, we discussed her superb report Petrodollar To Digital Yuan: China, the Gulf and the 21st Century Path to De-Dollarization and the perspective she offered proved another crucial piece of a puzzle I've been trying to assemble for a decade now:

> ***(Diana Choyleva): The Gulf states are adapting their economic and security frameworks—historically based on hydrocarbon exports, dollar-denominated trade, and security cooperation with the US—in response to evolving global conditions while maintaining key elements of existing relationships. Demographic shifts, the global energy transition, the technology revolution and the emergence of new economic powers are forcing a fundamental rethinking of development strategies. These domestic imperatives coincide with China's quest for energy security and its technological progress, including digital innovation.***
>
> ***The infrastructure of digital finance and trade—whether US or Chinese-led—creates lasting dependencies that are difficult to unwind. What began as pragmatic engagement with both systems could evolve into technological lock-in that shapes strategic alignment. Gulf states' involvement in initiatives like the mBridge digital currency platform offer immediate practical benefits but also create technological dependencies in an increasingly bifurcated global financial architecture.***
>
> ***The Gulf's evolving position offers crucial insights into how economic imperatives and technological innovation are reshaping traditional security relationships.***

The evolution of the Gulf States' position is vital to understand. Thankfully, Diana is on hand to help:

> ***(Diana Choyleva): The Gulf states' pursuit of economic transformation is unfolding against a backdrop of shifting geopolitical realities. Where once they would have confidently pursued renewal within the framework of a US-led military and financial order, they now face a more complex strategic environment.***
>
> ***US's increasing focus on strategic competition with China and its achievement of energy independence have reshaped its relationships with the Gulf states. Once balanced by strong economic interdependence, these partnerships have become more politically oriented, reflecting a shift toward geopolitical alignment rather than shared economic reliance.***
>
> ***The US security guarantee to the Gulf, anchored by Saudi Arabia's 1975 security-for-oil arrangement, has been a cornerstone of regional stability. However, US's newfound energy independence - thanks to shale gas - has fundamentally altered its strategic calculus. As the perceived "China threat" intensifies, the US has increasingly shifted its military focus and resources toward the Indo-Pacific region to counter China's expanding influence. This pivot has come at the expense of its traditional commitments in the Gulf, signaling a strategic realignment that prioritizes security concerns in the Asia Pacific over maintaining its historical military presence in the Middle East overall. Consequently, Gulf states are reassessing their reliance on US security guarantees in light of this evolving focus.***

These include the reduction of US missile defense systems in the Gulf region, the Obama administration's ground-breaking Iran deal (repudiated by the first Trump administration), and the perception that the US' responses to the 2019 attacks on Aramco oil processing facilities and the 2022 Houthi attacks on Abu Dhabi were muted at best. 6 7 The chaotic US withdrawal from Afghanistan in 2021 further reinforced impressions of declining US military presence.

Evidence of somewhat less-than-enthusiastic support for the US from the Gulf region in recent years (and, crucially, a lessening in the recycling of petrodollars) can be seen in the holdings of US treasuries and equities of both Saudi Arabia and the UAE (Fig. 13).

Meanwhile, no more than a cursory glance at the Gulf states' major trading partners for their only significant business line ought to help you understand that the motivations driving their alignment going forwards are very different to those which underpinned the entirety of the half-century-long petrodollar agreement (Fig. 14).

Fig. 13

Gulf State Holdings of US Equities & Treasuries ($bln)
2020 - 2024

Source: Enodo Economics, SEC, Argaam

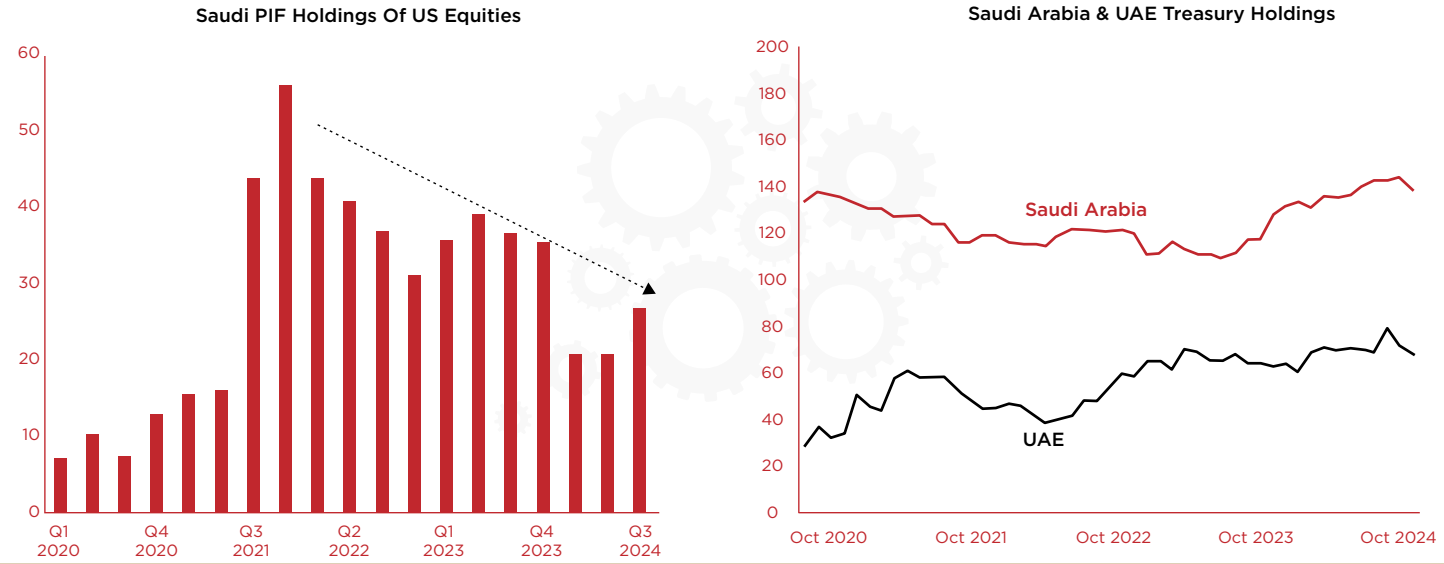


Fig. 14

Gulf Oil Exports By Destination (%)
2024

Source: Enodo Economics, CEIC

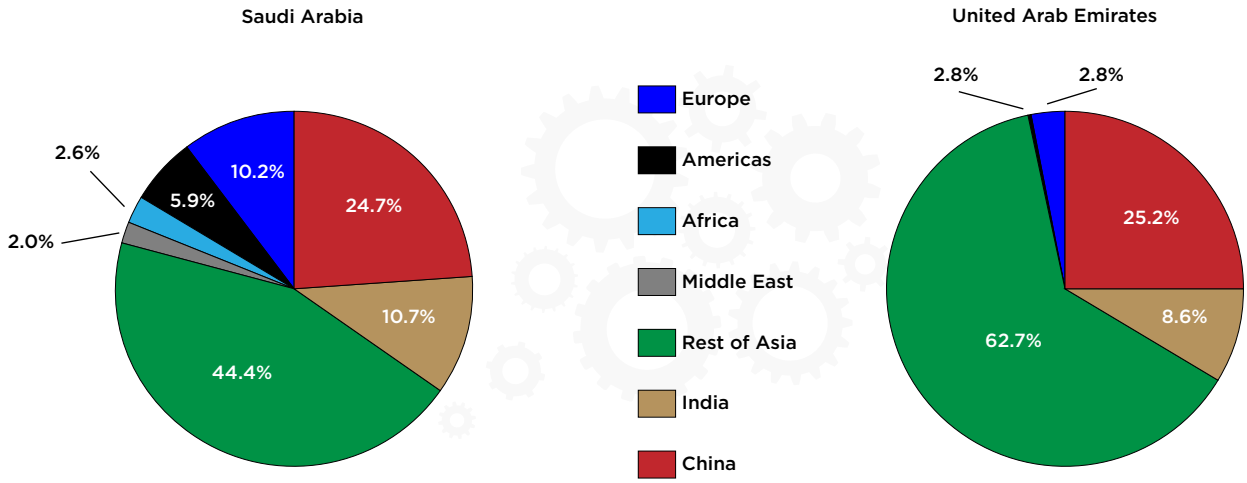
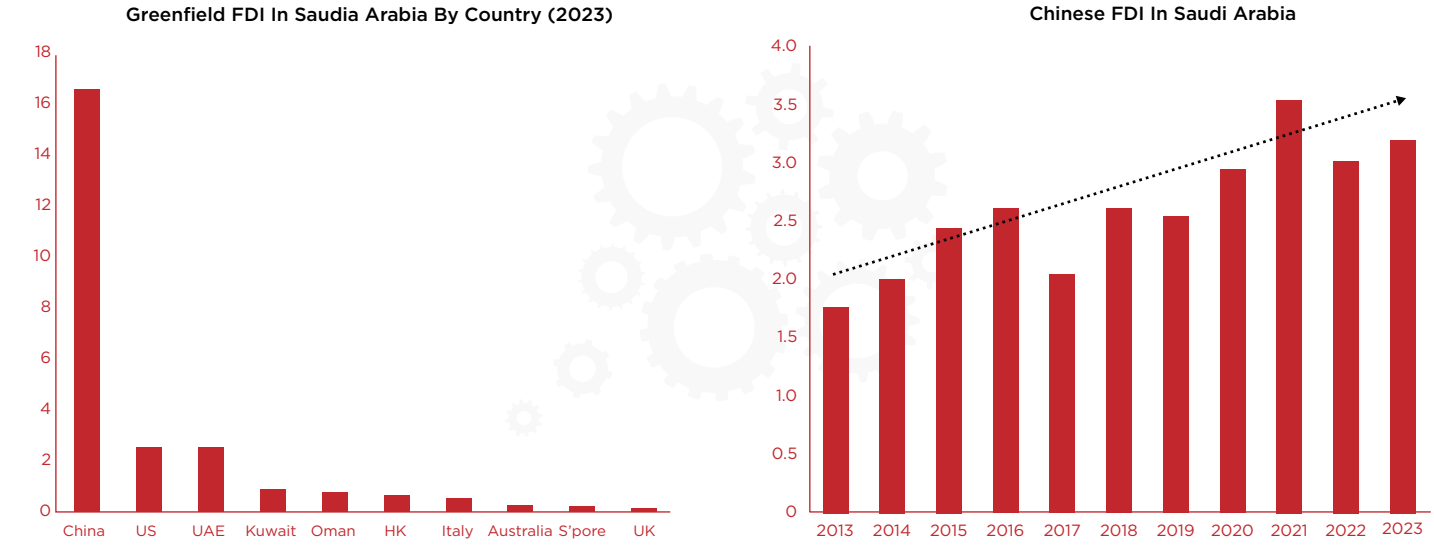


Fig. 15

Foreign Direct Investment (FDI) Into Saudi Arabia ($bln)
2013 - 2024

Source: Enodo Economics, Emirates NBD



Taking that a step further, we can see both the growth of Chinese FDI into Saudi Arabia and, importantly, the degree to which China has made itself by far the largest and most important source of funding for greenfield projects in the Kingdom (Fig. 15).

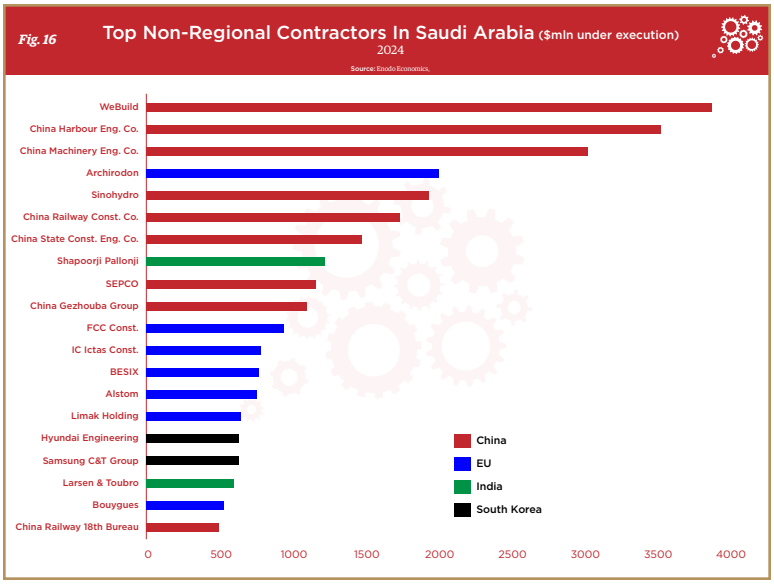
Here's Diana Choyleva again:

> ***(Diana Choyleva): The Gulf states find themselves navigating an increasingly complex strategic calculus. On one side stands their longstanding security relationship with the US – strained but still fundamental to regional stability. On the other side lies the economic reality of China.***
>
> ***China is the primary purchaser of Gulf oil and is a global manufacturing and technology powerhouse. Under Xi Jinping, it has transformed itself from merely a major trading partner into a self-reliant technological superpower.***
>
> ***This growing economic alignment builds upon a decade of careful diplomatic groundwork undertaken by Beijing. As its need for oil grew, Beijing has systematically deepened its political and diplomatic ties with Gulf states, creating the framework for today's expanding economic partnership. This has yielded rapidly expanding cooperation between the two sides, built on deepening integration between Chinese and Gulf enterprises, and growing investment flows from Gulf sovereign wealth funds into Chinese investments.***
>
> ***The ever-present oil industry is, of course, the primary vector of deepening Chinese investment, with Chinese state-owned oil and engineering firms playing a central role in recent refinery upgrades and expansion. Much of these have been financed by debt issued by Chinese banks, consolidating and tightening China's hold over the region's economic lifeblood.***
>
> ***Still, as they try to diversify away from their economic over-dependence on the oil industry, the Gulf states have found Chinese firms to be ready and willing partners.***

Indeed they have and, if we take a look at the largest foreign contractors working in Saudi Arabia, we find an interesting dynamic, with the Chinese essentially replicating the strategy that secured US influence over Central America post-WWII (Fig. 16).

Of course, Central America offered the US domestic insulation from the creeping threat of Communism... and bananas, but the Gulf States offer something far, far more important to the Chinese: energy (and it doesn't hurt that they're also slowly prising the region from grasp of the US).

It's this burgeoning alliance between China and



the Gulf States, built upon shared commercial interests, a natural energy supply/demand dynamic, geographical and cultural proximity and, increasingly, a shared desire for autonomy away from the growing weaponization of the US dollar and the unwanted pressure it allows the United States to apply to its 'friends.'

In its own moment of crisis in 1956, Great Britain saw up close how the United States was able (and willing) to leverage its rising strength and the UK's dependence upon its support to shift the entire global monetary order to its own advantage.

Now, seventy years after Suez, the United States finds itself, if not in a similarly weak position, then certainly facing a moment of potential crisis as a worthy adversary rears its head, bent upon securing its own advantage in a re-imagined monetary system.

China has built both infrastructure and influence alongside its allies in Asia and the Gulf and is in the process of converting that to its own advantage.

In part two of this edition of *Things That Make You Go Hmmm...* we'll look at what China has built, what it's trying to achieve and how it will likely go about that in a digital age that makes its aims far easier to achieve.

The battle for the bedrock of the global financial system has been quietly raging for years and, while it has been widely ~~understood~~ believed that the world can only function if there is a single system in place, we are, I suspect, about to find out that, while that may ultimately be correct, a second system is about to be introduced which will challenge the status quo in potentially seismic fashion.

No financial system endures forever. Not because they're badly designed, but because the world they serve inevitably changes.

The historical pattern is familiar. Britain didn't lose its empire at the moment political authority receded, but when financial flows no longer returned in the way they once had. Her formal influence endured after economic centrality had started to fade and the process wasn't sudden, but it also wasn't announced

It was decisive nonetheless.

Alrighty then. It's hard to believe we're at the end of yet another year and, while 2025 seems to have flown by, it somehow simultaneously feels as though it lasted a decade. Nevertheless, we have a bunch of interesting stories to get through before we bring down the curtain on an extraordinary twelve months.

We begin things in China where the country's trade dynamics are forcing Europe into something of an existential crisis. Staying in Europe, we discover the real cause for the bloc's decay and hear how the EU is freezing Russian assets yet again (what was it Einstein said about the definition of insanity?).

Japan offers us a canary in a coal mine of sorts (according to Barry Eichengreen, at least), we hear why we ought to worry about stablecoins and Howard Marks asks the all-important question: is it a bubble?

Michael Howell offers grist for the mill of this particular edition of *Things That Make You Go Hmmm...* when he explains how and why the global monetary system is bifurcating, while, in America, the AI race is well and

truly on and the darkest depths of winter lay ahead.

Our old friends at Tether are desperately continuing their quest for legitimacy (or at least to reach the all-important level where they are too big to be allowed to fail) by bidding for Italy's storied Juventus football club, we have three fascinating charts around tourism to the US, the UK's drastically-reduced per-capita GDP and Oracle's BIG bet on AI before we wrap things up with a chance to hear from Mike Green, Luke Gromen and Carson Block.

That's it from me for another year. Thank you, as always, from the bottom of my heart for supporting my work and allowing me to do what I love. My gratitude extends far beyond mere words.

I wish you and your families all the every best for the holiday season and health, happiness and success in whatever 2026 chooses to throw our way.

Until next year...

Before I let you go, just a quick reminder that tickets are now on sale for the upcoming Super Terrific Happy Day 2 which Steph Pomboy, Dave Iben and I will be hosting at the beautiful Vinoy Hotel in St. Petersburg, FL on February 17th 2026.

We have a stellar line-up of speakers again this year including Tom McClellan, Dr. Helen Messier, Dan Rasmussen, Andrew McDermott and Tom Hoenig plus a couple more who are yet-to-be-announced and a special mystery guest who will be unveiled at the event.

There are three different types of ticket packages available: SUPER, TERRIFIC and SPECTACULAR but they're selling fast, so don't miss out on a chance to join us for what promises to be another fabulous event.

Click on the button below to find out everything there is to know about everything you need to know and we'll look forward to seeing you there!!.

China forces reckoning in Europe as trade turns existential

Bloomberg

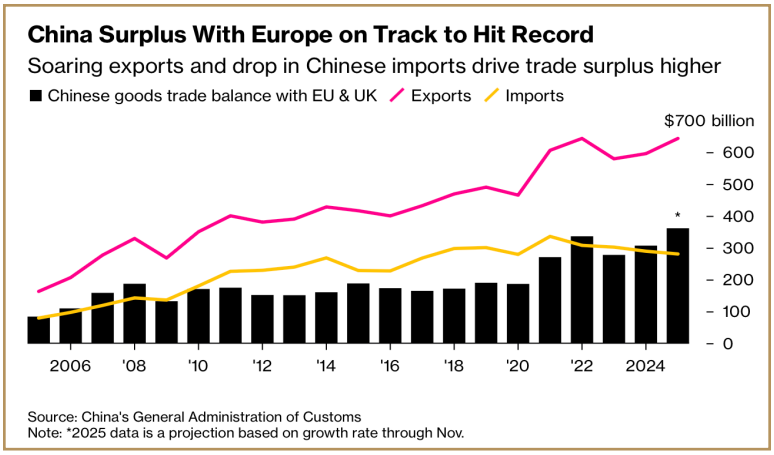
China's exports are putting it on a collision course with Europe.

French President Emmanuel Macron has branded the trade imbalance with China "unbearable," saying what's at stake now is "a question of life or death for European industry." European Commission President Ursula von der Leyen believes the bloc's ties with China "have reached an inflection point."

The scale of the imbalances with the European Union was thrown into stark relief days ago when Beijing disclosed its trade surplus with the bloc had widened to a record approaching $300 billion in 2025. The value of China's exports to the EU is now more than double its imports, as Chinese sellers divert goods facing levies in the US.

"The China shock in Europe is really starting to hit," said Andrew Small, director of the Asia program at the European Council on Foreign Relations. "What you've now had in recent months has been much greater levels of urgency, not all of it playing out in public, but serious crisis meetings taking place."

The result could be the biggest rethink of EU policy toward Beijing in at least a decade, according to Small, who previously advised von der Leyen on China. Sidetracked for years by the war in Ukraine and, more recently, by Donald Trump's tariffs, the EU is finally focusing on China, preparing what Small describes as a "pent-up" mix of measures.



The bloc unveiled a plan earlier this month to ensure its industries aren't overtaken by global rivals, as competition intensifies with the US and China. The European Commission, the EU's executive arm, has also proposed setting up an economic security hub to better navigate trade tensions and counter the threat of cheap products flooding the bloc's single market.

And it's expected to propose setting conditions around inbound investments such as technology transfers and the use of domestic content and value chains.

The wake-up call comes as other major economies erect trade barriers: Mexican lawmakers this week gave final approval for new tariffs on Asian imports.

Time is short for Europe. Economists at Goldman Sachs Group Inc. estimate competition from Chinese exports will cut gains in German, Spanish and Italian gross domestic product by 0.2 percentage point or more from next year through 2029.

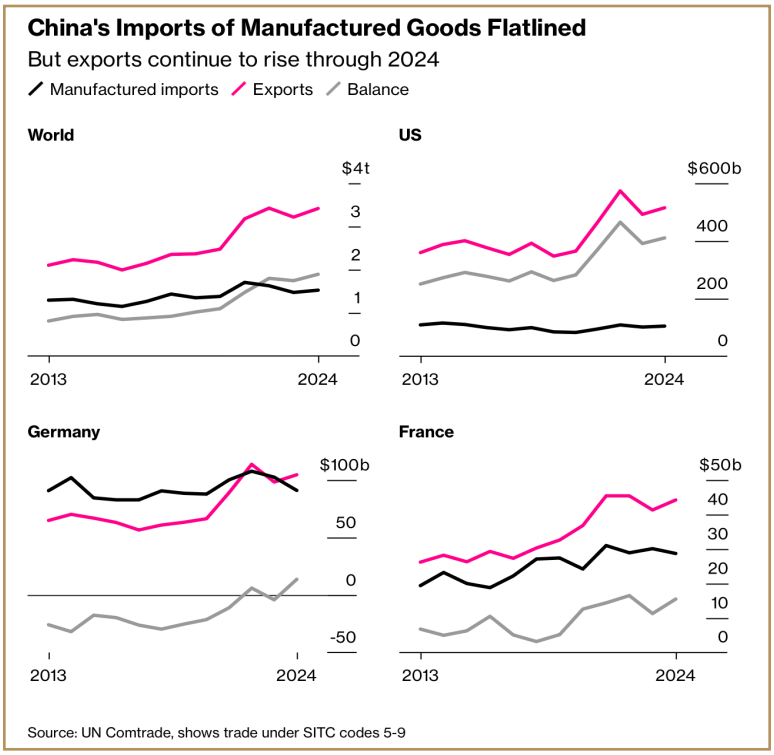
The fallout from China's exports might extend to almost a third of euro-area employment, according to economists at the European Central Bank, meaning it could possibly affect more than 50 million jobs.

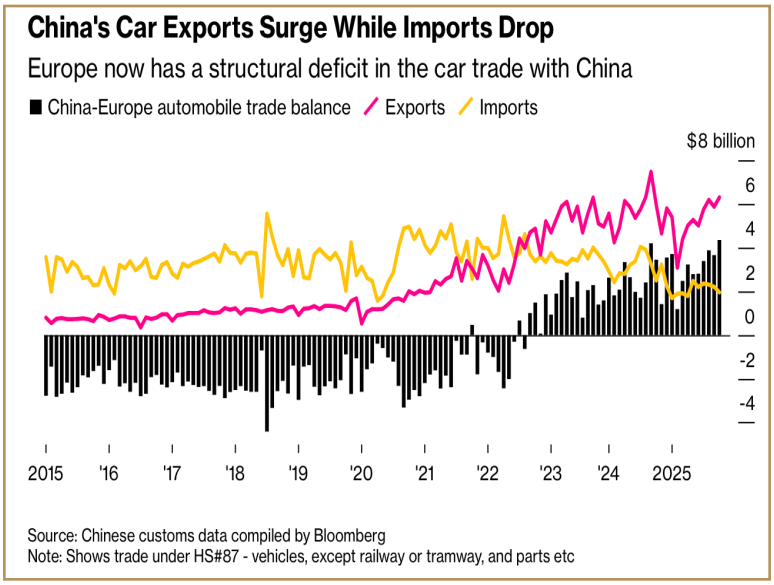
"External hostility toward goods exported by China will escalate, particularly in Europe," said Stephen Jen, chief executive of London-based hedge fund Eurizon SLJ Capital. "This configuration of explosive trade and a cheap renminbi cannot be sustained."

For China, there is little alternative. The EU's $20 trillion economy is among the few markets big enough to absorb the goods it used to ship to the US.

Over in Brussels, the risks of a confrontation became clear this year, when tensions over trade escalated between China and the US. Beijing then leveraged its dominance of rare earths, disrupting major industries from electric vehicles to wind turbines and causing numerous production stoppages at European companies.

While the EU committed at least €3 billion ($3.5 billion) over the next year to help sever its dependence on China's raw materials, in reality that'll take years to





have meaningful impact.

It's not just China's industrial strength that gives it an edge.

Propelling its exports is a currency that is undervalued in the view of many economists, making exports cheaper and imports more expensive. The yuan hit a decade low against the euro earlier this year despite the record trade surplus in Beijing's favor.

"One of the real reasons that Chinese exports are going so fast is that the renminbi is very significantly undervalued relative to the euro," said EU Chamber of Commerce in China President Jens Eskelund, using an alternative name for the currency. This acts as a "subsidy" for exports and suppresses Chinese consumers' purchasing power, he said.

For every container that Europe exports to China, four containers come back the other way, said Eskelund, adding that this imbalance is not just growing, but accelerating.

China's trade surplus with Europe took off during the pandemic, as people bought more goods to adapt to lockdowns and working from home.

Chinese firms simultaneously began to move up the value chain and started competing more with foreign companies in higher-tech sectors such as medical devices and high-end cars. With China's imports flat-lining over time, a re-acceleration of its exports has made the trading relationship ever more lopsided.

As a result China is now taking 7% of EU exports but supplying almost a quarter of all imports from outside the bloc. China's surplus with the EU and the UK now accounts for nearly a third of its total trade differential with the world, which exceeded $1 trillion for the first time.

The asymmetry means Europe's firms are losing sales to China, while having to contend with increased pressure at home from cheap goods. What's more, they also face greater competition in other overseas markets, as Chinese companies rapidly increase their shipments of cars and other goods to the rest of the world.

Germany is at the ground zero of the changing terms of trade with Beijing.

In 2019, China ran a $25 billion deficit with Europe's biggest economy. In the first 11 months of this year, that's flipped to a $23 billion surplus due to the collapse in imports.

The result for Germany is an economy stuck in a funk, battered by job cuts and increasing competition from China both at home and abroad. German industry has been cutting more than 10,000 jobs a month this year, according to federal statistics agency Destatis.

Combined with high energy prices and challenges such as an aging population, the weakness forced Chancellor Friedrich Merz's advisers to cut their growth forecast for Germany next year to below 1%.

China's advantage doesn't just exist in high-tech manufactured goods like electric vehicles, with its firms continuing to dominate in production of cheap consumer goods, clothing and shoes.

Shipments of cheap products from e-commerce sites have soared every year since the pandemic, and were up another 56% in the first 10 months of this year compared to the same period in 2024...

Few market observers understand the plumbing system of the global liquidity structure better than Michael Howell. The founder of CrossBorder Capital and GL Indexes in London specializes in analyzing liquidity flows.

In the past few weeks, we have seen signs of stress in the financial system and tensions in the repo market. How worrisome is this development?

It's very worrisome. Because it basically shows you that liquidity conditions are beginning to tighten worldwide. The fundamental problem that we're facing right now is that the Fed has stepped down its liquidity injections into markets. I'm not saying they have done this deliberately because that sounds rather sinister, but they are doing it with the full knowledge that it would create tensions.

What was the thinking within the Fed?

The Federal Open Market Committee has made a conscious decision to shrink the Fed balance sheet, to get the level of reserves in the U.S. banking system down and to withdraw liquidity from the system. It's crucial to understand that this happened while the Treasury General Account, which is the balance that the U.S. Treasury holds at the Federal Reserve, was going through a significant rebuilding phase. If the TGA is rebuilt, the effect is a withdrawal of liquidity. As you remember, during the first half of 2025, the debt ceiling forced the Treasury to run down the TGA, which caused liquidity to spike. Since summer, though, they have rebuilt the TGA. And unfortunately for them, the government shutdown in October meant that they could not spend any more money, and so the amount in the TGA exceeded $1 trillion. That amounted to a big withdrawal of liquidity.

Weren't the policymakers at the Fed aware of this effect?

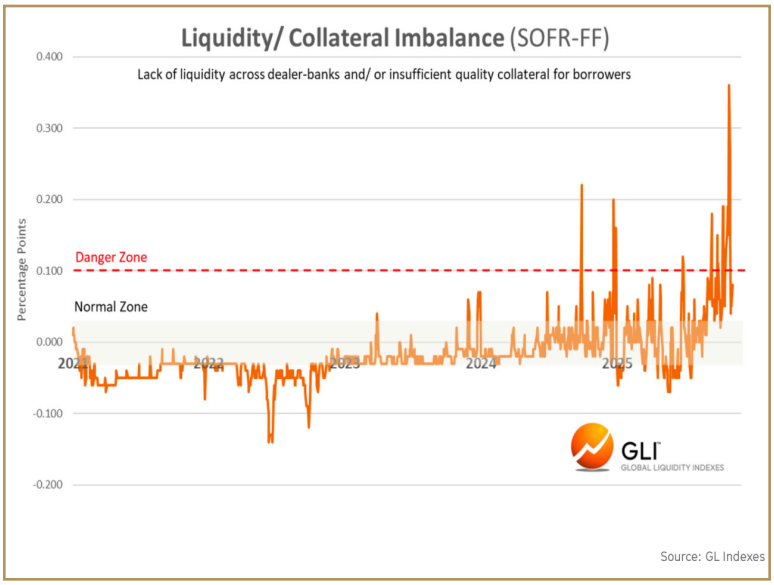
Well, you can divide the FOMC into three groups. First, you have the orthodox central bankers, like Chairman Jay Powell or John Williams, President of the New York Fed. Then you have the Trumpites, such as Governor Stephen Miran. Third, there are what I would call the monetary plumbers. Those are the ones who really understand how liquidity moves through the system. The most prominent member of that group is Lorie Logan, President of the Dallas Fed. The plumbers are a minority in the FOMC. At the moment we have a situation where the repo markets are struggling. That's an inconvenience for the Fed, it's not yet a big problem. But it could develop into a bigger problem.

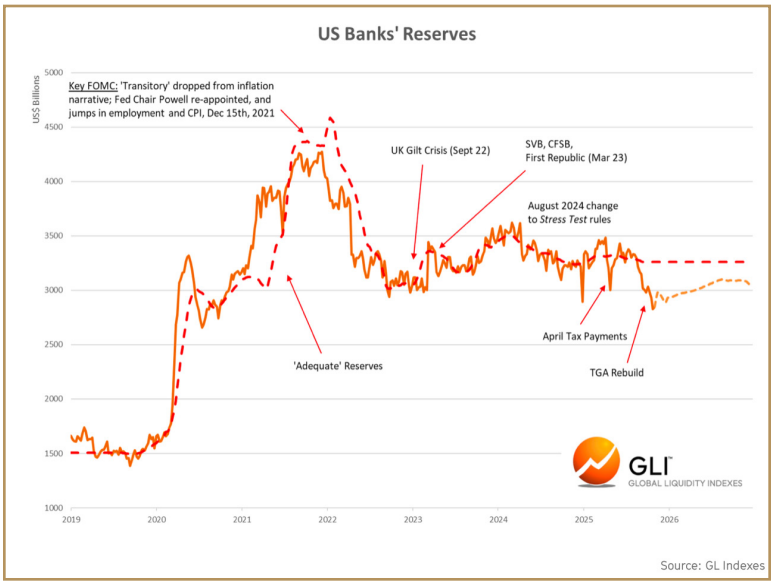
What signs are you looking at that show you that liquidity is too tight?

You can see the problem in the repo market, specifically in the spread between the Secured Overnight Financing Rate and the Fed Funds Rate. The former is the collateral-based interest rate, and it should normally be slightly below the Fed Funds Rate, which shows the uncollateralized lending rate. But currently, we see spikes where the SOFR rises significantly above the FFR, sometimes by more than 10 basis points, at times even 25 basis points. That's a big spread in the repo market. One can say that the Fed is losing control of interest rates at the front end of the curve. Linked to this is the rising number of trade fails among primary dealers. More trade fails mean more volatility in the market.

And why is that a problem?

Hedge funds have become a very important source of funding in the Treasury market. The Fed did an exercise several weeks ago which showed that hedge





funds last year bought well over $1.5 trillion of U.S. Treasury debt. Given the fact that the new issuance was about $2 trillion, you get the idea that hedge funds were important in supporting the bond market, through a strategy that is called the basis trade. If you start to see wobbles, like repo rates going up and the number of trade fails rising, hedge funds may get skittish and start to reverse out of the basis trade, which could make the bond market spike.

One could say that when it comes to the plumbing of the financial system, the Fed has learned their lesson from 2019 when they had to deal with a big repo crisis. They won't let anything bad happen. Would you agree?

They certainly don't want anything bad to happen because there is so much risk in that. But I'm not sure they understand what's happening right now. Among the three constituents within the FOMC, the monetary plumbers, those who know that we need liquidity, are in the minority. The orthodox central bankers, meanwhile, are still inclined not to pay a lot of attention to liquidity. New York Fed President Williams allegedly prides himself on saying that he never looks at a Bloomberg screen. Jay Powell is not a monetary economist by background. The orthodox central bankers are more focused on interest rates. And the second group, the Trumpites, say they want to cut interest rates, but at the same time they also want the Fed balance sheet to shrink. This means they accept that bank reserves are falling.

And you're saying that bank reserves have fallen too low now?

Yes. Bank reserves have fallen too fast since August. For the U.S. economy to function well, bank reserves need to be around $3.25 trillion, and right now they are sitting at a little more than $2.8 trillion.

Isn't that a paradox, cutting interest rates while, at the same time, consciously withdrawing liquidity?

Yes. The view of the Trumpites like Stephen Miran seems to be that if you cut interest rates, you deliver for the average voter in America. By getting interest rates and by extension mortgage rates down, you help the guy on Main Street. The dollar will also weaken in a lower interest rate environment. That's where they are coming from. They don't want the Fed balance sheet expanding again, because that only pushes asset prices up, creating this big divide between Main Street and Wall Street.

Powell will be replaced at the helm of the Fed next May. What change do you expect?

The Trumpites will get stronger. The appointees that we'll get on the FOMC are more inclined to the Miran line, i.e. they will aim for a smaller balance sheet and lower interest rates. But the problem is Wall Street needs liquidity. When liquidity goes down, markets start to wobble. That's what we are seeing now.

Investors hope that the FOMC will reverse course at its next meeting on December 10th. The quantitative tightening has ended on December 1st, and markets

expect a 25 basis point rate cut. There is even talk of renewed quantitative easing. What do you make of that?

It's certainly possible, but I doubt that they will deliver enough. Just to get bank reserves to where they should be would need additional liquidity in the order of something like $250 billion. We would have to get back to full scale QE to get liquidity to where it should be.

Is there a chance that we will see a renewed rundown in the TGA, which would give liquidity support?

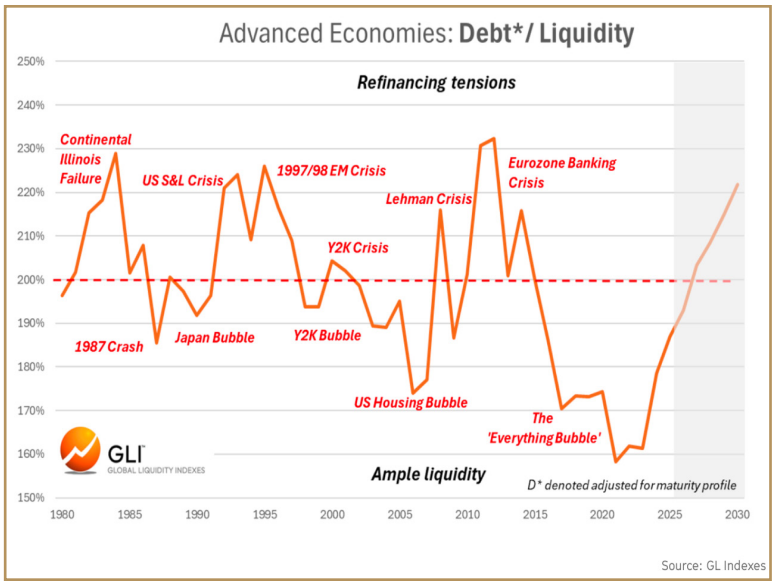
I doubt it. At the maximum, I would estimate $100 to 150 billion. The point is that the TGA has to remain at around $800 to 850 billion. Why? Because the TGA is implicitly mandated to cover about five days of government spending. The Treasury is issuing lots of short-term bills, which constantly need to be refinanced. Every week, roughly $500 billion of Treasury Bills need to be rolled. Plus another $125 billion in longer term coupon Notes. So they have $625 billion of Treasury debt to roll each week in auctions. They have to have a TGA balance commensurate with that, on top of their traditional spending demands and interest payments. Add all this up, and you get to a figure of about $800 billion as a cushion in the TGA. They won't be able to run this down much from here.

Could a liquidity crisis jolt the Fed into action?

Right now, all I can say is that the monetary plumbers in the FOMC don't get much to say. It is possible that we see a crisis that will force the hand of the Fed. You see, many market participants don't understand how liquidity works. Financial markets today are much more about debt refinancing than they are about raising new capital. The textbook model of the capital market is that it is used to raise capital for investment projects. That's no longer true. Today, the whole nature of the financial system is refinancing previous debts. 70 to 80% of all transactions are basically debt refinancing in some form. If you refinance debt, you need balance sheet capacity in the financial system, and that means liquidity. Liquidity itself, paradoxically, is collateralized through old debt. So liquidity needs debt, and debt needs liquidity. This system can derail in two ways: One, you get an inability to turn liquidity into debt, which is the refinancing problem, and the other is a problem of turning debt into liquidity, which is a collateral problem.

So debt and liquidity need to be in an equilibrium?

Exactly. If you have too much debt relative to liquidity, you get refinancing tensions, and they spill over into financial crises. Every financial crisis you can think of in the last few decades has been a refinancing crisis. And if, on the other hand, you have too much liquidity relative to debt, you get asset bubbles, because the valve for too much liquidity is higher asset prices. In the past few years, we have had the latter situation: Too much liquidity, which led to inflated asset prices and what we could call the Everything Bubble.



And now the pendulum is swinging back?

Yes, I think so. During the Covid years, corporations and governments issued a lot of debt, and a big chunk of this debt needs to be refinanced between 2026 and 2030. A debt maturity wall lies ahead. Debt refinancing needs liquidity, but at exactly this time, the Fed is not accommodating these needs. Unless the Fed starts to inject significantly more liquidity, we have a problem.

What does that mean for the general economic picture for 2026?

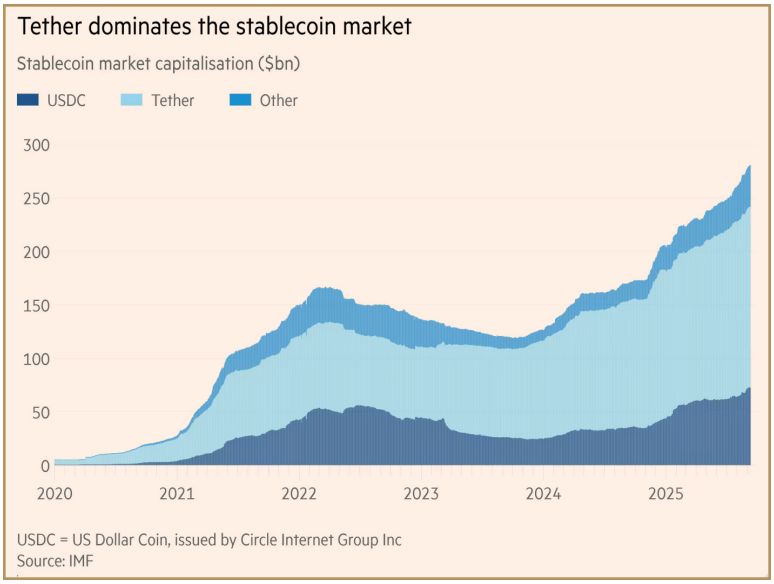
This may sound paradoxical, but in terms of the real economy, I expect an acceleration in the U.S. While the Fed is not accommodative enough, the Treasury is. Think of it like a form of QE, but conducted by the Treasury, which is boosting fiscal spending by issuing gigantic amounts of short-term bills. On top of that,

we have this huge AI capex boom coming through. We could be seeing somewhere between $0.25 to 0.5 trillion in extra capex. We can debate whether ultimately that's good or unproductive capex, but right now, that's a meaningless question. Because right now, we get the spending. So I expect the U.S. economy to get a boost next year. It may start to pick up steam through 2026, which is exactly what the administration would want given the midterm elections. But there are two problems connected with that...

A few months ago, the father-in-law of one of my sons, who lives in New York state, sent what was, for him, a significant sum of money to his family in England. The money never arrived. Worse, it was impossible to discover what had happened to it. His bank contacted the intermediary it used, but was told that the destination bank in the UK, one of the country's largest, would not respond to queries. I asked colleagues what might have happened and was advised that it might have something to do with money laundering. Meanwhile, my in-law was distraught. Then, after two months, the money suddenly reappeared in his account. He remains entirely ignorant of what happened in between.

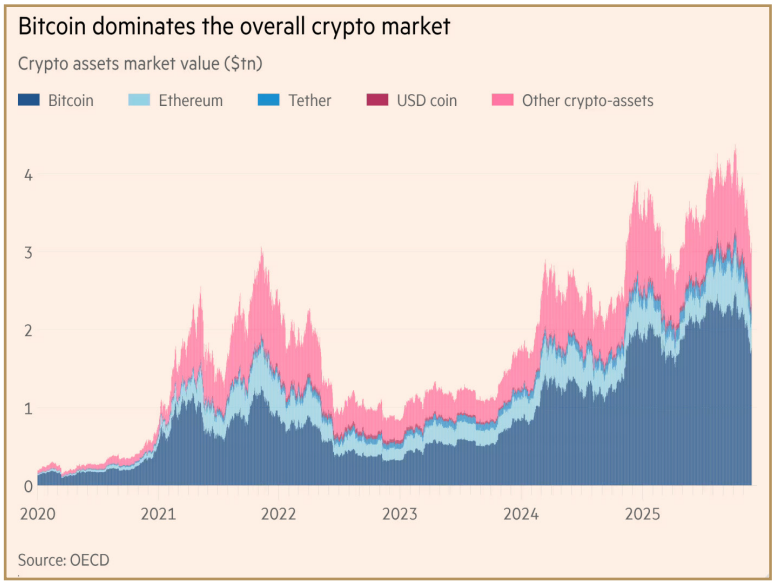
Such an event is utterly remote from anything I have experienced when transferring money between the UK and the EU. On this side of the pond, transfers have been uniformly reliable and fast. This might be a reason for Americans to welcome the use of "stablecoins" as an alternative to their banking system. Daniel Davies has noted two others: the relatively high cost of payments made via credit cards (which are around five times those in Europe!) and the extortionate cost of cross-border remittances. Both reflect the failure to regulate powerful US oligopolies.

The FT's Gillian Tett suggested a different motivation for the Trump administration's welcoming stance on stablecoins in an article last month. Scott Bessent, US Treasury secretary, has a problem: the enormous



volume of US Treasury debt the US needs the world to hold at modest interest rates. One solution, she notes, is to promote the widespread use of dollar-denominated stablecoins, not so much domestically, but everywhere else. This, as Tett notes, would be good for the US government.

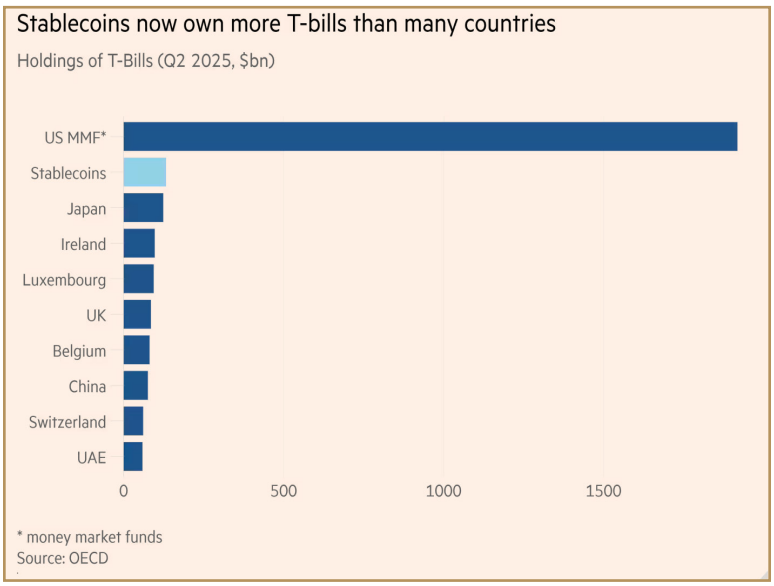
Yet none of these are good reasons for welcoming dollar stablecoins. As Hélène Rey of the London Business School argues, "For the rest of the world, including Europe, wide adoption of US dollar stablecoins for payment purposes would be equivalent to the privatization of seigniorage by global actors." This then would be yet another predatory move by the superpower. Alternatively, the US could shift towards a less costly payment system and less profligate government. But neither is likely.



In all, stablecoins — assets presented as digital alternatives to fiat money, especially US dollars — seem to have a bright future. Already, as Tett notes, "players such as Standard Chartered predict that the stablecoin sector will grow from $280bn to $2tn by 2028".

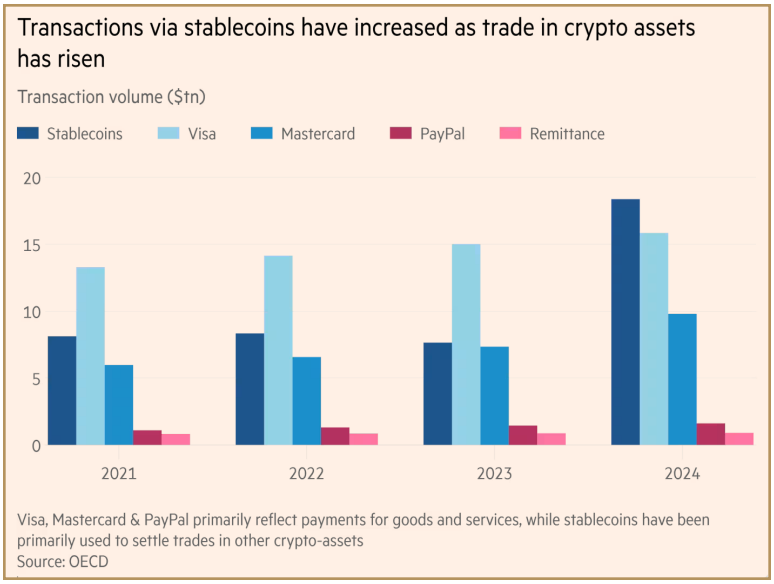
The future of stablecoins might indeed be bright. But should it also be welcomed by people other than the issuers, criminals of various kinds and the US Treasury? No.

Yes, stablecoins are far more stable than, say, bitcoin. But their purported "stability" is likely to prove a "con", relative to that of a dollar in cash or a bank.



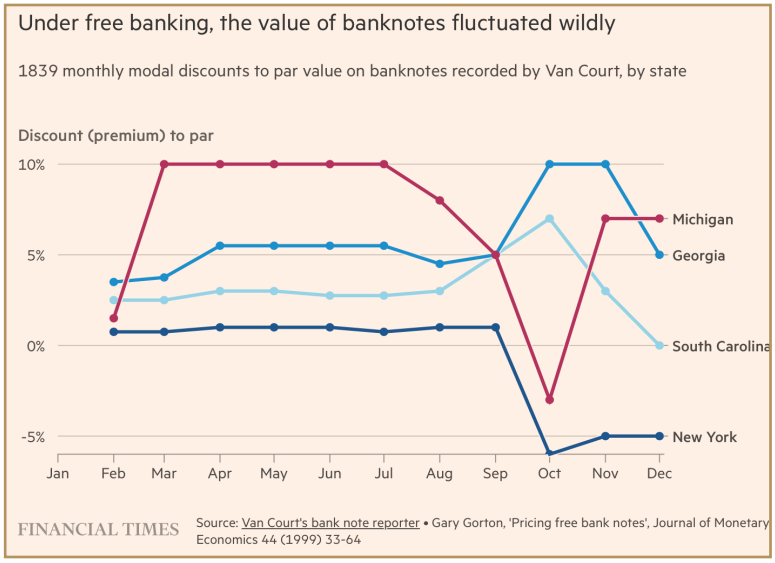
The IMF, OECD and Bank for International Settlements have all registered serious concerns. Interestingly, the latter welcomes the idea of "tokenisation": thus, "By bringing together tokenised central bank reserves, commercial bank money and financial assets into the same venue, a unified ledger can harness tokenisation's full benefits."

Yet the BIS is also concerned that stablecoins will fail to meet "the three key tests of singleness, elasticity and integrity". What does this mean? Singleness describes the need for all forms of a given money to be exchangeable with one another at par, at all times. This is the foundation of trust in money. Elasticity means the ability to deliver payments of all sizes without gridlock. Integrity means the ability to curb financial crime and other illicit activities. A central role in all this is played by central banks and other regulators.



Stablecoins, as now operated, fall far short of these requirements: they are opaque, easily usable by criminals and of uncertain value. Last month, S&P Global Ratings downgraded Tether's USDT, the most important dollar stablecoin, to "weak". This is not a trustworthy money. Private monies have often failed in crises. That is very likely to be true of stablecoins, too.

Let us assume then that the US is going to promote the use of lightly regulated stablecoins, partly in order to enhance the dominant role of the US dollar and so help finance its huge fiscal deficits. What should other countries do? The answer is to defend themselves as best they can. This is particularly true for European countries. After all, with its new national security strategy, the US has made quite clear its open hostility towards democratic Europe.



So, European countries need to consider how they might introduce stablecoins in their own currencies that are more transparent, better regulated and safer than what the US is now likely to produce. The Bank of England's approach seems a model of good sense: just last month, it introduced a "proposed regulatory regime for sterling-denominated systemic stablecoins", arguing that the "use of regulated stablecoins could lead to faster, cheaper retail and wholesale payments, with greater functionality, both at home and across borders." This seems to be the best starting point.

The people now in charge of the US are very much enamoured with the Big Tech motto of "move fast and break things". In the case of money, this could be disastrous. Yes, there are reasons to exploit the possibilities of new technologies for creating faster, more reliable and safer monetary and payments system. The US certainly needs this. But a system that makes fraudulent promises of stability, facilitates irresponsible fiscal policy, and opens the door to criminality and corruption is not what the world needs. We should resist it...

European leaders are furious at President Trump following his recent derogatory comments about their Continent. This is becoming an instructive diplomatic fiasco, even if it's one in which Dr. Trump botches his diagnosis of the Continent's most serious problems.

The Administration's National Security Strategy last week stirred outrage by warning that America's European allies face "civilizational erasure." Mr. Trump's foreign-policy panjandrums mean primarily that mass immigration and deepening political illegitimacy are sapping Europe's vim and vigor. Mr. Trump followed this week by describing Europe as "weak" and "decaying."

The strategy, a brainchild of Vice President JD Vance and his circle, implies the U.S. may withdraw from its longstanding security cooperation with Europe if Washington decides Europe is no longer worth defending. A particular threat concerns the North Atlantic Treaty Organization. The strategy paper warns that mass (read: Muslim) migration means some NATO members could within a few decades be majority non-European.

Messrs. Trump and Vance have a point. The European Union does too many things (foreign policy, environmental regulation and the like) badly that it shouldn't do at all. What it's supposed to do, such as creating a Continent-wide free-trade bloc, it does poorly.

European voters are angry about their leaders' failures to get a grip on a migration crisis now entering its second decade. They're frustrated with the increasing prosperity gap between Europe and the U.S., and with Europe's frailty in the face of foreign challenges such as Russia's war on Ukraine. Worst of all, they see that their leaders' first instincts are to suppress contrary opinions, which is why free speech is again a hot debate in Europe.

Some of this bespeaks the lack of confidence in European civilization the Trump Administration observes. Much of this traces to a loss of belief in the superiority of Western values, including guilt over imperialism and destructive 20th-century wars.

But the Trump diagnosis ignores the biggest threat to Europe's well-being. That is Europe's generous social-welfare states and the cascading fiscal, economic and social ills they create.

Government social expenditure in the U.S. accounted for 19.8% of GDP in 2024, according to data from the Organization for Economic Cooperation and Development. In France the figure was 30.6%, in Germany 27.9%, and in Italy 27.6%. This share will rise as populations age. These columns recently documented the severity of the old-age entitlement problem in France and Germany especially.

This fact explains much of what ails Europe. Large welfare states require large tax bills to fund them, which is why government revenue reaches 47% of GDP in France, 41% in Germany, and 43% in Italy but 27% in the U.S. That level of taxation saps incentives for innovation and entrepreneurship. Generous welfare states also discourage work, which partly

explains why Europe's labor markets are so sclerotic.

Meanwhile, European governments, taxed to the hilt and increasingly indebted, find it difficult to spend more on defense. Hence the Continent's inability to shape events in Ukraine, embarrassing leaders and voters and deepening the sense of ennui caused by economic underperformance.

The question is why Messrs. Trump and Vance stress migration and culture more than these fiscal and economic facts. Perhaps because Mr. Trump doesn't want to reform America's own entitlement state. Mr. Vance often speaks as if he wants to expand the government's role, as if welfare checks and bureaucracy can restore national elan and social unity.

Reforming welfare is politically difficult. It's far easier to denounce migrants and European cultural decadence. Especially when the U.S. is on a similar, if slower, path to welfare-state sclerosis.

Immigration is a manageable challenge, now that Europe is starting to grapple with it. Washington could also be a positive influence on Europe, as Reagan's policy example was in the 1980s. Mr. Trump's demand for more defense spending will require welfare reforms that would benefit everyone.

But an irony of the Trump-Vance rhetoric is that it could make most of Europe's problems worse. The domestic political allies they want to cultivate in Europe, such as Germany's Alternative for Germany (AfD) or France's National Rally, are big-state, anti-economic-reform parties, and often are instinctively anti-American to boot. This isn't the way to make friends or spur a European revival...

The EU froze indefinitely €210bn of Russian sovereign assets held in the bloc on Friday as Kyiv and its European allies sought to strengthen their hand at a critical phase in US-orchestrated peace talks.

The freezing paves the way for a loan to be raised against the assets to prop up Ukraine's defence. EU leaders still have to overcome strong objections from Belgium, where the assets are mostly held, at a summit next week.

Moscow fired back, filing a lawsuit against Euroclear, the Brussels-based depository holding most of the assets, which may allow Russia to seize the company's assets held inside the country.

The moves came as the Trump administration has ratcheted up the pressure on Kyiv to sign a peace deal with Russia by Christmas on largely unfavourable terms first drawn up between Washington and Moscow.

European leaders have closed ranks with Ukraine as it seeks to avoid being forced into what many Ukrainians and Europeans regard as capitulation.

President Volodymyr Zelenskyy is due to travel to Berlin on Monday to meet German Chancellor Friedrich Merz and other European leaders. Zelenskyy said they would discuss the security guarantees that European capitals would provide Ukraine as part of a peace settlement.

Ukrainian negotiators, supported by European officials, have sought to improve the terms of the US-brokered peace proposal, grasping for points of leverage while also considering once unthinkable concessions.

A revised peace proposal drawn up by Ukrainian and European officials and sent to Washington this week envisages Ukraine joining the EU as soon as 2027, an accelerated timetable that would rip up the bloc's established accession procedure.

Intensive diplomacy was under way to establish "common ground" between Ukrainians, Europeans and Americans on a new version of the deal that could then be presented to Russia, said a French official.

Yuri Ushakov, foreign policy adviser to President Vladimir Putin, said: "When we do see it, I sense that we're not going to like a lot of it."

While the EU made its move on Russian assets, Zelenskyy made a surprise visit on Friday to the

frontline city of Kupiansk, in eastern Ukraine, which Moscow claimed to have captured weeks ago. The Ukrainian army was pushing Russian forces back, Zelenskyy said, claiming its resistance there would strengthen Ukraine's hand in talks.

"This is exactly how it works: all our strong positions inside the country become strong positions in discussions about ending the war," he said.

Still, Russian forces continue to advance along other axes across the 1,200km frontline, heaping pressure on Ukraine's war-weary army.

European officials remain highly sceptical that Russia will agree to anything that falls short of their maximalist objectives, which include subjugation of Ukraine.

Zelenskyy has said Ukraine is discussing with US officials the details of a possible "free economic" or "demilitarised" zone in Donetsk province, which Moscow is insisting Ukraine surrender as the price of any deal. He has ruled out handing over territory, but suggested that Ukrainian forces could pull back from the contact line in the area if Russian forces did the same and Ukraine received strong security guarantees.

French foreign minister Jean-Noël Barrot said Zelenskyy "has shown for the last nine months his willingness to create the conditions for a peace deal that is both fair and lasting, which is not a capitulation. It is now up to Vladimir Putin to take the last step and put an end to this imperialist and colonial war..."

Ours is a remarkable moment in world history. A transformative technology is ascending, and its supporters claim it will forever change the world. To build it requires companies to invest a sum of money unlike anything in living memory. News reports are filled with widespread fears that America's biggest corporations are propping up a bubble that will soon pop.

During my visits to clients in Asia and the Middle East last month, I was often asked about the possibility of a bubble surrounding artificial intelligence, and my discussions gave rise to this memo. I want to start off with my usual caveats: I'm not active in the stock market; I merely watch it as the best barometer of investor psychology. I'm also no techie, and I don't know any more about AI than most generalist investors. But I'll do my best.

One of the most interesting aspects of bubbles is their regularity, not in terms of timing, but rather the progression they follow. Something new and seemingly revolutionary appears and worms its way into people's minds. It captures their imagination, and the excitement is overwhelming. The early participants enjoy huge gains. Those who merely look on feel incredible envy and regret and – motivated by the fear of continuing to miss out – pile in. They do this without knowledge of what the future will bring or concern about whether the price they're paying can possibly be expected to produce a reasonable return with a tolerable amount of risk. The end result for investors is inevitably painful in the short to medium term, although it's possible to end up ahead after enough years have passed.

I've lived through several bubbles and read about others, and they've all hewed to this description. One might think the losses experienced when past bubbles popped would discourage the next one from forming. But that hasn't happened yet, and I'm sure it never will. Memories are short, and prudence and natural risk aversion are no match for the dream of getting rich on the back of a revolutionary technology that "everyone knows" will change the world.

I took the quote that opens this memo from Derek Thompson's November 4 newsletter entitled "AI Could Be the Railroad of the 21st Century. Brace Yourself," about parallels between what's going on today in AI and the railroad boom of the 1860s. Its word-for-word applicability to both shows clearly what's meant by the phrase widely attributed to Mark Twain: "history rhymes."

Understanding Bubbles

Before diving into the subject at hand – and having read a great deal about it in preparation – I want to start with a point of clarification. Everyone asks, "Is

there a bubble in AI?" I think there's ambiguity even in the question. I've concluded there are two different but interrelated bubble possibilities to think about: one in the behavior of companies within the industry, and the other in how investors are behaving with regard to the industry. I have absolutely no ability to judge whether the AI companies' aggressive behavior is justified, so I'll try to stick primarily to the question of whether there's a bubble around AI in the financial world.

The main job of an investment analyst – especially in the so-called "value" school to which I subscribe – is to (a) study companies and other assets and assess the level of and outlook for their intrinsic value and (b) make investment decisions on the basis of that value. Most of the change the analyst encounters in the short to medium term surrounds the asset's price and its relationship to underlying value. That relationship, in turn, is essentially the result of investor psychology.

Market bubbles aren't caused directly by technological or financial developments. Rather, they result from the application of excessive optimism to those developments. As I wrote in my January memo On Bubble Watch, bubbles are temporary manias in which developments in those areas become the subject of what former U.S. Federal Reserve Chairman Alan Greenspan called "irrational exuberance."

Bubbles usually coalesce around new financial developments (e.g., the South Sea Company of the early 1700s or sub-prime residential mortgage-backed securities in 2005-06) or technological progress (optical fiber in the late 1990s and the internet in 1998-2000). Newness plays a huge part in this. Because there's no history to restrain the imagination, the future can appear limitless for the new thing. And futures that are perceived to be limitless can justify valuations that go well beyond past norms – leading to asset prices that aren't justified on the basis of predictable earning power.

The role of newness is well described in my favorite passage from a book that greatly influenced me, A Short History of Financial Euphoria by John Kenneth Galbraith. Galbraith wrote about what he called "the extreme brevity of the financial memory" and pointed out that in the financial markets, "past experience, to the extent that it is part of memory at all, is dismissed as the primitive refuge of those who do not have the insight to appreciate the incredible wonders of the present." In other words, history can impose limits on awe regarding the present and imagination regarding the future. In the absence of history, on the other hand, all things seem possible.

The key thing to note here is that the new thing understandably inspires great enthusiasm, but bubbles are what happen when the enthusiasm reaches irrational proportions. Who can identify the boundary of rationality? Who can say when an optimistic market has become a bubble? It's just a matter of judgment.

Something that occurred to me this past month is that two of my best "calls" came in 2000, when I cautioned about what was going on in the market for tech and internet stocks, and in 2005-07, when I cited the dearth of risk aversion and the resulting ease of doing crazy deals in the pre-Global Financial Crisis world.

- First, in neither case did I possess any expertise regarding the things that turned out to be the subjects of the bubbles: the internet and sub-prime mortgage-backed securities. All I did was render observations regarding the behavior taking place around me.

- And second, the value in my calls consisted mostly of describing the folly in that behavior, not in insisting that it had brought on a bubble.

Struggling with whether to apply the "bubble" label can bog you down and interfere with proper judgment; we can accomplish a great deal by merely assessing what's going on around us and drawing inferences with regard to proper behavior.

What's Good About Bubbles?

Before going on to discuss AI and whether it's presently in a bubble, I want to spend a little time on a subject that may seem somewhat academic from the standpoint of investors: the upside of bubbles. You may find the attention I devote to this topic excessive, but I do so because I find it fascinating.

The November 5 Stratechery newsletter was entitled "The Benefits of Bubbles." In it, Ben Thompson (no relation to Derek) cites a book titled Boom: Bubbles and the End of Stagnation. It was written by Byrne

Hobart and Tobias Huber, who propose that there are two kinds of bubbles:

> *. . . "Inflection Bubbles" – the good kind of bubbles, as opposed to the much more damaging "Mean-reversion Bubbles" like the 2000 's subprime mortgage bubble.*

I find this a useful dichotomy.

- The financial fads I've read about or witnessed – the South Sea Company, portfolio insurance, and sub-prime mortgage-backed securities – stirred the imagination based on the promise of returns without risk, but there was no expectation that they would represent overall progress for mankind. There was, for example, no thought that housing would be revolutionized by the sub-prime mortgage movement, merely a feeling that there was money to be made from backing new buyers. Hobart and Huber call these "mean-reverting bubbles," presumably because there's no expectation that the underlying developments would move the world forward. Fads merely rise and fall.

- On the other hand, Hobart and Huber call bubbles based on technological progress – as in the case of the railroads and the internet – "inflection bubbles." After an inflection-driven bubble, the world will not revert to its prior state. In such a bubble, "investors decide that the future will be meaningfully different from the past and trade accordingly." As Thompson tells us:

> The definitive book on bubbles has long been Carlota Perez's Technological Revolutions and Financial Capital. Bubbles were – are – thought to be something negative and to be avoided, particularly at the time Perez published her book. The year was 2002 and much of the world was in a recession coming off the puncturing of the dot-com bubble.
>
> Perez didn't deny the pain: in fact, she noted that similar crashes marked previous revolutions, including the Industrial Revolution, railways, electricity, and the automobile. In each case the bubbles were not regrettable, but necessary: the speculative mania enabled what Perez called the "Installation Phase," where necessary but not necessarily financially wise investments laid the groundwork for the "Deployment Period." What marked the shift to the deployment period was the popping of the bubble; what enabled the deployment period were the money-losing investments. (All emphasis added)

This distinction is very meaningful for Hobart and Huber, and I agree. They say, "not all bubbles destroy wealth and value. Some can be understood as important catalysts for techno-scientific progress."

But I would restate as follows: "Mean-reversion bubbles" – in which markets soar on the basis of some new financial miracle and then collapse – destroy wealth. On the other hand, "inflection bubbles" based on revolutionary developments accelerate technological progress and create the foundation for a more prosperous future, and they destroy wealth. The key is to not be one of the investors whose wealth is destroyed in the process of bringing on progress.

Hobart and Huber go on to describe in greater depth the process through which bubbles finance the building of the infrastructure required by the new technology and thus accelerate its adoption:

> Most novel technology doesn't just appear ex nihilo [i.e., from nothing], entering the world fully formed and all at once. Rather, it builds on previous false starts, failures, iterations, and historical path dependencies. Bubbles create opportunities to deploy the capital necessary to fund and speed up such large-scale experimentation – which includes lots of trial and error done in parallel – thereby accelerating the rate of potentially disruptive technologies and breakthroughs.
>
> By generating positive feedback cycles of enthusiasm and investment, bubbles can be net beneficial. Optimism can be a self-fulfilling prophecy. Speculation provides the massive financing needed to fund highly risky and exploratory projects; what appears in the short term to be excessive enthusiasm or just bad investing turns out to be essential for bootstrapping social and technological innovations . . . A bubble can be a collective delusion, but it can also be an expression of collective vision. That vision

> becomes a site of coordination for people and capital and for the parallelization of innovation. Instead of happening over time, bursts of progress happen simultaneously across different domains. And with mounting enthusiasm . . . comes increased risk tolerance and strong network effects. The fear of missing out, or FOMO, attracts even more participants, entrepreneurs, and speculators, further reinforcing this positive feedback loop. Like bubbles, FOMO tends to have a bad reputation, but it's sometimes a healthy instinct. After all, none of us wants to miss out on a once-in-a-lifetime chance to build the future.

In other words, bubbles based on technological progress are good because they excite investors into pouring in money – a good bit of which is thrown away – to carpet-bomb a new area of opportunity and thus jump-start its exploitation.

The key realization seems to be that if people remained patient, prudent, analytical, and value-insistent, novel technologies would take many years and perhaps decades to be built out. Instead, the hysteria of the bubble causes the process to be compressed into a very short period – with some of the money going into life-changing investment in the winners but a lot of it being incinerated.

A bubble has aspects that are both technological and financial, but the above citations are from the standpoint of people who crave technological progress and are perfectly happy to see investors lose money in its interest. "We," on the other hand, would like to see technological progress but have no desire to throw away money to help bring it about.

Ben Thompson ends this discussion by saying, "This is why I'm excited to talk about new technologies, the prospect for which I don't know." I love the fact that he's excited by future possibilities and at the same time admits that the shape of the future is unknown (in our world, we might say "very risky").

Assessing the Current Landscape

Now let's get down to what we used to call "brass tacks." What do we know? First, I haven't met anyone who doesn't believe artificial intelligence has the potential to be one of the biggest technological developments of all time, reshaping both daily life and the global economy.

We also know that in recent years, economies and markets have become increasingly dependent on AI:

- AI is responsible for a very large portion of companies' total capital expenditures.
- Capital expenditures on AI capacity account for a large share of the growth in U.S. GDP.
- AI stocks have been the source of the vast majority of the gains of the S&P 500.

As a Fortune headline put it on October 7:

> ***75% of gains, 80% of profits, 90% of capex – AI's grip on the S&P is total and Morgan Stanley's top analyst is 'very concerned'***

Further, I think it's important to note that whereas the gains in AI-related stocks account for a disproportionate percentage of the total gains in all stocks, the excitement AI injects into the market must have added a lot to the appreciation of non-AI stocks as well.

AI-related stocks have shown astronomical performance, led by Nvidia, the leading developer of computer chips for AI. From its formation in 1993 and its initial public offering in 1999, when its estimated market value was $626 million, Nvidia briefly became the world's first company worth $5 trillion. That's appreciation of around 8,000x, or roughly 40% a year for 26+ years. No wonder imaginations have been fired...

A prospective rise in Japanese interest rates could indicate that not only Japan, but also other heavily indebted economies, including the United States, could face sharply higher yields on government bonds. The only way out for Japan is to boost economic growth; but for the US, it is to raise taxes.

Earlier this month, global bond markets were rocked by remarks from Bank of Japan Governor Kazuo Ueda suggesting that the BOJ would soon weigh whether to raise interest rates. The resulting sell-off in the US bond market raised yields on ten-year and 30-year US Treasuries sharply.

Normally, mild comments by a mild-mannered Japanese central banker are not enough to perturb US and global markets. But the BOJ has a well-earned reputation as a canary in a coal mine. In February 1999, it cut interest rates to zero in a desperate effort to fend off deflation, anticipating the zero-interest-rate policies of other central banks when they, too, confronted the specter of deflation.

Today, the BOJ's prospective move in the other direction could be indicating that not just Japan but also other heavily indebted economies, including the United States, are about to face sharply higher yields on government bonds, with all the difficulties that entails.

The Japanese government's total debt as a share of GDP is on the order of 230%, twice that of the US. Net debt, subtracting the Japanese government's assets, is a more manageable, if still high, 130%. Unfortunately, many of those government assets, such as landholdings, are illiquid, so they are of little comfort to public debt managers.

None of this was a problem so long as interest rates – and therefore debt-service payments – were at or near zero. But if interest rates now rise to, say, 4%, debt service will begin to strain the government budget. The BOJ has kept rates low through a combination of bond buying and yield-curve control, whereby it targets specific maturities where the debt is concentrated. Now that inflation is back, this de facto subsidy is ending.

There are no easy solutions to Japan's debt problem. Taxes as a share of GDP are above the OECD average. An elderly population complicates any effort to cut pension and healthcare costs. And Japan, like other countries, now faces geopolitical pressure to spend more on defense.

The only way out is to boost the debt ratio's denominator: GDP. Prime Minister Sanae Takaichi's fiscal stimulus is designed to jumpstart growth. Subsidies for electricity bills, cash handouts to households with children, and payments to government-licensed bear hunters (you read that right) will stimulate demand.

The question is how to stimulate supply. More immigration would help. So would policies that raise female and elder labor-force participation, comprehensive reskilling for older workers, deregulation of the service sector, and tax incentives for technology upgrading by small and medium-size enterprises. On the supply side, however, Japan is moving slowly, if at all.

So, the new government's supplementary budget threatens to worsen the fiscal position instead of improving it. It may be premature to panic, but Mrs. Watanabe, that mythical investor in Japanese government bonds, now appears fully awake to the risks.

Moreover, what happens in Japan doesn't stay in Japan. It is transmitted to the US via two channels. First, if yields on Japanese government bonds go up, they will become more attractive relative to US Treasuries, putting upward pressure on US interest costs. Second, the more difficulty Japan has in managing its debt, the more investors will begin worrying about other heavily indebted countries.

Fortunately, the US has an easy way out. In the US, unlike Japan, taxes as a share of GDP are below the OECD average. Closing even half the gap between the US and advanced-economy averages would eliminate the primary budget deficit (excluding interest payments) and stabilize its debt ratio.

Of course, tax increases are for the US what supply-side reform is for Japan: a political third rail. President Donald Trump's administration has futilely sought to address the deficit problem by cutting government spending. The result has been to cut muscle rather than fat, gutting government and university spending on research and public services essential for productivity growth. The legacy of Trump's "Department of Government Efficiency" has been zero progress in curtailing the deficit.

Democrats are now focused, appropriately, on the affordability crisis caused by higher food, health-care, and housing costs. But they also need to worry about the mortgage costs that will follow from higher

interest rates, and about the politically toxic inflation that will occur on what they hope will be their watch, after 2028.

A tax on billionaires won't close the budget gap and fend off these dangers. What is needed is a broad-based but progressive increase in taxes, together with that fabled closing of loopholes such as carried interest.

Implementing this will require a very different Congress and a very different president. A crisis often is needed to trigger the kind of political realignment that can deliver both. A debt crisis, during which inflation and interest rates shoot up, would certainly qualify. The question is whether US politics can realign in the absence of one...

Earlier this year, the only remaining Democrat commissioner left on the US Securities and Exchange Commission eviscerated the "Jenga-like" dismantlement of the financial regulator. Yesterday she went even further.

Caroline Crenshaw stressed that this wasn't a "farewell address"; her term as an SEC commissioner actually ended last year. She's only still in the building because of an 18-month grace period that ends this month, and the Trump administration's refusal to nominate a replacement for the slot reserved for a Democrat.

However, her Brookings speech yesterday – titled The Rubble and the Rebuild – still read as a final primal scream at the remarkable evisceration of financial regulation that has happened in 2025.

"The appetite to deregulate has been rapacious," she noted:

> ***It has been unsettling to see how precipitously one Commission is willing to undo the work of the Commission that came before it – all without a single notice-and-comment rulemaking to date.***
>
> ***I'm concerned that the fundamental precepts upon which our markets have been built – tenets that have, by and large, kept our markets safe for both issuers and investors alike – are being eroded. I fear that the very core of our intricate market structure is under attack.***
>
> ***And instead of safeguarding our markets for investors to fund their retirements in safe and sustainable ways, we are moving in a direction where markets start to look like casinos. The problem with casinos, of course, is that in the long run the house always wins.***

Crenshaw then describes what she calls "the rubble" caused by the SEC – four malignant trends that "embody a sort of chaos that I think has characterised the past year".

These are the devaluation of investor rights in the name of making IPOs easier; reducing transparency with lighter corporate reporting requirements and the SEC shunning public comments; pushing ordinary investors into private markets without any safeguards; and the remarkable lack of SEC enforcement actions and lower SEC penalties even when the agency does act.

> ***The appetite to deregulate has been rapacious; the analysis of the costs and benefits of our policies has been non-existent; and, the repercussions, I would argue, could be dire.***
>
> ***We live in an echo chamber where politicians and policymakers make their own truth through repetition. But, the markets have a way of correcting themselves – not always immediately, but over time. So, I think the true advisability of these policies will reveal themselves eventually. I certainly wouldn't be alone in analogising the trend toward deregulation in the current environment to the period prior to the stock market crash in 1929.***
>
> ***...Of late, we have frequently been told that today is a "new day" at the Commission. But anyone aware of our place in the calendar knows that with each successive day the nights grow longer. I fear that the darkest depths of winter still lie ahead for America's capital markets.***

Crenshaw spent the last bit of her speech talking about

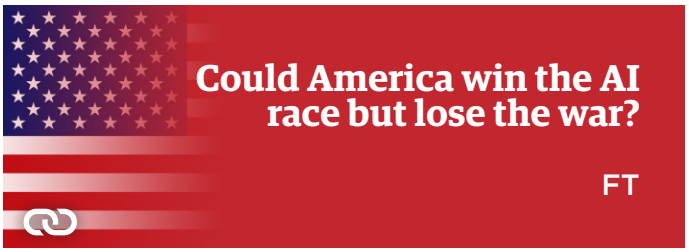
the future rebuild, but this was long on sweeping principles and short on specifics, and reads almost like an oblique application to be a SEC chair under any future Democrat president.

Yet even by the standards of US officials — with endemic politics often leading to very dramatic public hand-wringing — this is pretty remarkable stuff.

Moreover, it is probably the last time we'll hear something like this from an SEC commissioner for a while.

Crenshaw has to leave the building by the end of the year. With the Trump administration not naming a successor — or a successor to Democrat commissioner Jaime Lizarraga, who resigned last year — it means we will probably have an SEC without a commissioner from the minority party for the first time on record (aside from a brief six-month window back in 2008).

Minority commissioners have little power at the SEC, aside from voicing public dissent like this. But it seems even dissent is not to be brooked these days...



Over the past year, major US tech companies have spent more than $350bn on AI-related infrastructure, with projections of over $400bn for 2026. This far exceeds the spending of any other nation — most notably China, where total investment is closer to an estimated $100bn.

For many in the west, it may be reassuring that we have companies bold enough and capital markets deep enough to dominate a spending contest. If artificial intelligence is — as prophesied — the one ring to rule them all, then it would seem the west has the future in hand.

That is the optimistic story. Yet there is another possibility: that Silicon Valley's obsession with AI could mean winning the AI race but losing a broader contest for economic pre-eminence. That follows because the US has gone all-in on AI, while China is spreading its bets across several plausible futures. It all depends on the bet on AI being the right one.

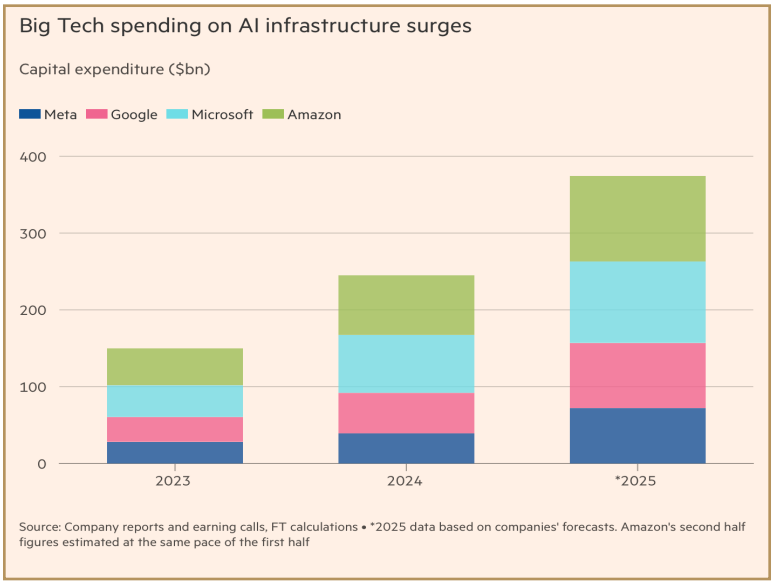
Despite all the talk of an existential AI race, China is somewhat less committed to AI than sometimes portrayed. Beijing regularly describes AI as a "national strategic priority" and has invested to avoid falling too far behind. But the state and its major companies are spending much more money to secure dominance in other domains, such as electric vehicles, batteries, robotics, solar panels, wind turbines and other forms of advanced manufacturing. These sectors may be less glamorous, but their returns are far less speculative.

It is the US that is truly infatuated with AI, with investments influenced by goals that are as mystical as they are commercial, especially the pursuit of Artificial General Intelligence and "the singularity". There is a strong belief in continued exponential progress — a rarity in the history of technology. The deeper one digs, the more otherworldly it becomes, among both AI proponents and doomsayers. The concentrated, monopolised nature of the US tech sector adds to the risk: with so much spending power in so few hands, the danger of groupthink grows.

What to do? If the pay-off from AI is uncertain, the prudent strategy would involve diversification and hedging. But American venture capital is as fixated on AI as the tech platforms themselves, and financial markets have rewarded the current course. The public sector could hedge, but the US — under Trump — has cut back support for clean-energy investment, leaving the national tech strategy looking like a large wager on a single horse.

Today's AI spending, while impressive, is undeniably a frontloaded bet on one vision of the future. It may prove inspired and visionary. Or it could be remembered as an overdone fixation on a technology whose utility is narrower than advertised. Its failure to deliver could also be the trigger for a destabilising stock crash that leaves the west behind.

Seen from some distance, the American tech strategy looks like a straightforward syllogism: AI is the most important technology of the 21st century; it is extremely expensive to build; therefore, whoever spends the most will be the dominant civilisation of the future. But any syllogism stands or falls with its premises. The key question is whether today's version



of AI is in fact the most important path to prosperity and a better future.

That turns out to be more of a leap of faith than many assume. The business case has long been somewhat vague, and on closer examination much of what Silicon Valley presents as the goals of AI has a distinctly fantastic flavour. "We believe Artificial Intelligence is our alchemy, our Philosopher's Stone," writes venture capitalist Marc Andreessen. He and Silicon Valley's other "accelerationists" believe achieving artificial intelligence is the paramount goal for humanity, a kind of secular rapture. Believers think AI can solve most of our problems: just last week, Google DeepMind's Demis Hassabis suggested AI could invent free renewable clean energy and discover the cure for most diseases; humanity is then "travelling to the stars and spreading consciousness to the galaxy".

In some ways, the American AI race looks not unlike the race to build the grandest cathedrals in late medieval Europe. Then, the motives were a mixture of pride, economics and a sincere religious belief the structures would bring humanity closer to salvation. The byproduct was some extraordinary architecture — but also financial ruin for cities such as Beauvais and Cologne, overwhelmed by their own ambition.

Inside Silicon Valley, the finish line of the "race" is the achievement of AGI: the moment when machines acquire humanlike cognitive versatility. Believers argue that once AGI arrives, it will trigger further breakthroughs — the "law of accelerating returns". A superintelligence may then reach "the singularity", a concept popularised by Ray Kurzweil and Vernor Vinge, ushering in a regime described by the latter as "as radically different from our human past as we humans are from the lower animals". Accelerationists hope this superintelligence will yield a "radical abundance". As Sam Altman once said, once general AI is invented, "poverty really does just end".

Andreessen, the author of a "techno-optimist manifesto", puts it his way: we are "poised for an intelligence takeoff that will expand our capabilities to unimagined heights". The technology, he claims, is "liberatory of human potential. Liberatory of the human soul, the human spirit. Expanding what it can mean to be free, to be fulfilled, to be alive." It follows, on this view, that slowing AI development is not merely unwise but immoral. "[A]ny deceleration of AI will cost lives. Deaths that were preventable by the AI that was prevented from existing is a form of murder."

By comparison, at least, the way the Chinese government speaks about AI is more modest. Yes, China's economic leadership views AI as a priority and has boldly claimed it seeks to lead the world by 2030. Yet the rhetoric lacks the eschatological tone common in Silicon Valley. Chinese economic planners appear more interested in AI as a tool for industrial processes than as a means of creating a superintelligence that will reach the singularity. The State Council's 2025 "AI+" initiative is focused entirely on efficiency-enhancing applications rather than intelligence explosions.

There is another important difference. China is banking far more heavily on simpler, lower-cost open-source AI models. In the US, most of the leading "frontier" AI models are secret and proprietary, in part as a business model and in part due to the apocryphal fears that the wrong actors could trigger human extinction. The smaller, lower-cost Chinese models may be seeking, in that sense, to be the more nimble 1970s Toyota rivals to the giant American cars produced by General Motors.

More importantly, China is hedging its bets by investing heavily in a wide range of other technologies that might reasonably be described as "the future". In 2024, the country invested an estimated $940bn in clean-energy capex, broadly defined as renewables, electricity grids and energy storage (batteries), dwarfing its AI investments. In these sectors, AI is meant to be a complement — the glue rather than the

structure.

While China's overall economy remains weaker than it was in the 2010s, elements of this broader strategy seem to be bearing fruit. Last year, 70 per cent of the world's EVs were manufactured in China. China also accounts for roughly 80-85 per cent of global solar photovoltaic manufacturing, and more than 75 per cent of all global battery production. If we set AI aside for a moment and assume that these technologies represent the future, it is clear who is ahead.

The popular notion of an international AI race, and of a Chinese state gripped by existential obsession with AI, seems to come more from American sources than Chinese. In a 2020 paper, for example, political scientist Graham Allison and former Google chief executive Eric Schmidt argued that China desperately needs to develop AI to prevent the collapse of its state-planned system. "The command of 1.4 billion citizens by a Party-controlled authoritarian government is a herculean challenge," they wrote. "AI could give the Party…a claim to advance a model of governance — a national operating system — superior to today's dysfunctional democracies." In essence, the need for social control was said to leave China no choice but to invest heavily in AI.

The theory is clever, but whether it is right is another question. What is clear is that the Party believes economic performance is essential to its survival, but, as described above, that conviction has led it towards a diversified strategy, not a single bet on artificial intelligence. Frontier AI, the most expensive form, has not been the main emphasis, and China appears to think it can do what it needs with "good enough" AI. The success of DeepSeek — a decent domestic copy of ChatGPT — may validate that strategy.

The US-China "AI race" does serve another function: it is an excellent messaging and lobbying tool for the American tech industry. Schmidt, Mark Zuckerberg and others have insisted that government intervention such as antitrust enforcement would handicap the US in this end-of-times battle for civilisation itself. The idea of a race also justifies extraordinary levels of spending, lest someone else swoop in and take the prize.

It is probably more accurate to say that the real AI race is an American race that dates from the 2010s — with China added to the narrative later. In the US, this contest moved from academia to commerce when Google began aggressively buying up AI talent and firms, including Britain's DeepMind and Geoffrey Hinton's DNNresearch. The race was joined in 2015 when Elon Musk and Sam Altman agreed on the need to fund non-profit OpenAI as a rival to Google.

And that American race was from the beginning more eschatological than commercial. Ray Kurzweil in 2005 set 2045 as the date for the coming singularity; hired by Google, he in 2017 asserted that "we will multiply our effective intelligence a billion fold by merging with the intelligence we have created". Musk, meanwhile, became obsessed with the dangers that superintelligent AI "could render humanity extinct". From the beginning, extravagant, end-of-history rhetoric has been the hallmark of the field.

Unlike in China, the American doubling and tripling down on AI has coincided with a move away from investment in clean-energy technologies and a reduction in support for basic research in other fields. The Trump administration has worked to de-incentivise electric vehicle uptake and clean-energy investment, and in response GM and Ford have reduced their investments in EVs and battery production.

The US has further reduced spending on basic science, now at roughly one-third of its 1960s level, and has waged rhetorical war on major academic research universities such as Harvard and Columbia. With the federal government reducing its commitment to science and clean energy, the American bet on the future increasingly looks like artificial intelligence or bust.

I would not deny the possibility that the accelerationists are right and that we may yet achieve an AGI that works for the betterment of humanity. If so, this period will be remembered for its brilliant grasp of what was needed to elevate humanity into a new and better age. But that outcome is far from certain, and both history and physics suggest caution…

Cryptocurrency giant Tether has made a €1.1bn all-cash offer to acquire Italian football club Juventus, in a bid underscoring the burgeoning ambitions and newfound riches of the stablecoin provider.

El Salvador-based Tether said it is proposing to pay €2.66 per share for the 65.4 per cent stake in the club held by Exor, the holding company of the billionaire Agnelli family which has controlled the club since 1923.

Pending regulatory approval, Tether said it would then move to buy the remainder of shares at the offer price.

Juventus shares were worth €2.19 a piece at market close on Friday with a market capitalisation of just under €925mn. The Tether offer values the club at €1.1bn.

People close to Exor said it did not intend to sell its stake "to Tether or to any other party". One of the people added: "Juventus is not for sale."

Tether has built an 11.5 per cent stake in Juventus over the course of this year and the bid is set to further inflame tensions between the company's leadership, who hail from Italy, and Exor's chief executive John Elkann.

Tether chief Paolo Ardoino said in a statement on Friday evening: "Juventus has always been part of my life."

"I grew up with this team. As a boy, I learned what commitment, resilience, and responsibility meant by watching Juventus face success and adversity with dignity."

The news comes at the end of a difficult week for Exor. The group's decision to sell its Italian media assets has prompted labour strikes at La Stampa and La Repubblica newspapers and harsh criticism from several Italian politicians.

Elkann and his family are staunch Juventus supporters and have owned the club, based in their hometown of Turin, for more than 100 years. A stake was floated on the Milan stock exchange in 2001.

People close to Elkann say he does not intend to disengage from his home country as critics infer, and Juventus and other important Italian assets are not on sale. Though Juventus has faced turbulence over the past few years, "the family is committed to turning the club's luck around," one of the people said.

Tether is the world's largest issuer of stablecoins, a digital token pegged to the value of the US dollar. It has roughly $185bn outstanding of its token USDT and it largely derives income on the interest collected on US Treasuries backing the token.

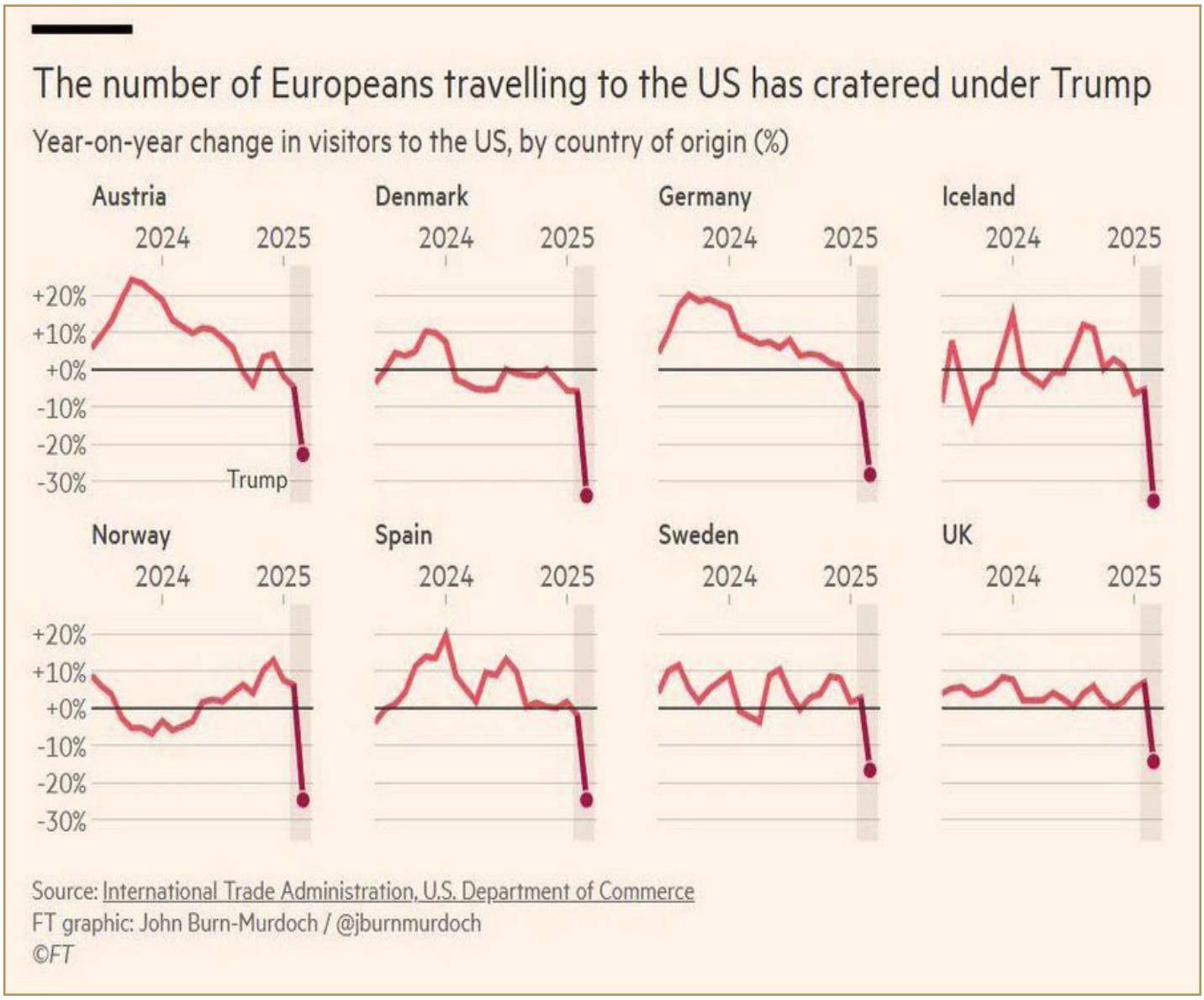
Tether made $10bn in the first nine months of 2025 and expects to book around $15bn in profits for the full year. It is in the midst of raising $15-20bn at a $500bn valuation from strategic investors and is mounting an expansion in the US.

The group has ploughed its profits into investments in early-stage technology start-ups as well as media companies.

Juventus last won Serie A, the top level of Italian football, in 2020. It suffered major losses during the coronavirus pandemic and sold its outstanding player Cristiano Ronaldo in 2021.

An accounting scandal also rocked the club, which separately failed to launch a breakaway European Super League in 2021. Former president Andrea Agnelli, a central actor in trying to establish the ESL, departed the following year.

The club has fallen behind its main rivals, having watched the likes of Inter Milan, AC Milan and Napoli win the Scudetto, or league title, in recent years...



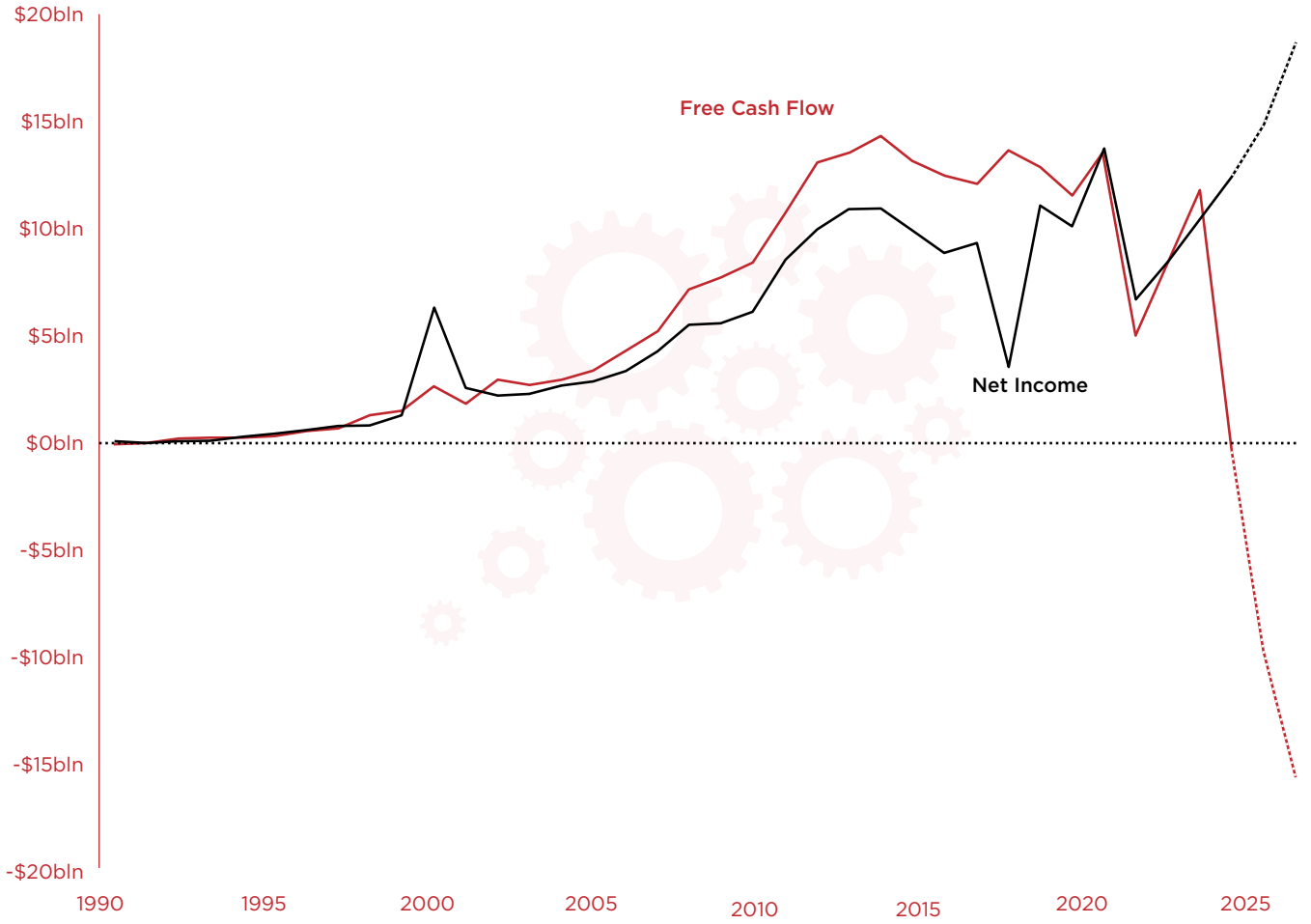
European tourism to the United States has dropped precipitously since Donald Trump's second term began...

Wow!

Oracle Free Cash Flow vs Net Income ($bln)

1990 - 2027e

Source: Chartr, Bloomberg



Well, Oracle's massive expansion into the world of AI is clearly set to be a company-making (or company-breaking) bet. Their projected capex over the next two years is astonishing, and their free cash flow is set to dive dramatically but I'm sure they'll make it all up on the back end.

If they don't? Well... that wouldn't be good.

WORDS THAT MAKE YOU GO HMMM...

MIKE GREEN

My buddy Mike Green recently published an extraordinary three-part piece on the reality of what constitutes the poverty line in the United States today.

The response has been amazing and the discussion around it charged, to say the least.

Here, Mike discusses his work with Peter McCormack. Superb.

LUKE GROMEN

Much of my own thinking about dedollarisation has been influenced by conversations with my great mate Luke Gromen. In this excellent podcast with Jack Farley, Luke argues that the US is facing the "Mother of All Crises": a forced choice between losing the AI race to China or destroying the US Treasury market. He also explains why the electrical grid is the ultimate bottleneck, why Bitcoin is flashing a warning signal for 2026, and the mathematical path to $15,000 gold.

CARSON BLOCK

Here's one for the books—a long idea from Carson Block. Yes, you read that correctly, and it's a doozy.

Presenting at the Sohn Conference in London, here's Carson doing Carson things and providing some typically diligent, detailed research into a long idea in the junior gold mining space.

They say if you live long enough, you'll see everything. Here's proof, and it's superb!

On the left, Petty Officer 1st Class Joe Friedman On the right, Senior Chief Petty Officer Keith Arneson, both members of the United States Navy band.

These two fine gentlemen (and fine musicians) decided to settle an argument once and for all so here, for your enjoyment, is Dueling Jingle Bells.

Enjoy!

Much to his chagrin, Grant Williams has reached 40 years in finance.

Over that period, he has held senior positions at a number of investment banks and brokers including Robert Fleming, UBS, Banc of America and Credit Suisse in locations as diverse as London, Tokyo, New York, Hong Kong, Sydney and Singapore.

From humble beginnings in 2009, *Things That Make You Go Hmmm...* has grown to become one of the most popular and widely-read financial publications in the world.

Grant is a senior advisor to Vulpes Investment Management in Singapore, an advisor to Matterhorn Asset Management in Switzerland and also one of the founders of Real Vision—an online, on-demand TV channel featuring in-depth interviews with the brightest minds in finance.

A regular speaker at investment conferences across the globe, Grant blends history and humour with keen financial insight to produce unique presentations which have been enthusiastically received by audiences wherever he has travelled.

To find out more about Things That Make You Go Hmmm... please visit:

www.grant-williams.com