February 13, 2025

Morning Briefing

On Tariffs, IPOs & AI Tools

Check out the accompanying chart collection.

Executive Summary: Trump 2.0's various new tariffs have multiple aims. Regarding China, the administration hopes that the additional 10% across-the-board tariff on all imports from the country will spur the Chinese government to slow the flow of fentanyl into the US. Jackie reports on how China has responded. … Also: Investors have bid up stocks in the S&P 500 Financials sector in hopes that many will benefit from Trump 2.0's business-friendly tax and capital market policies. Will the IPO market continue its gradual rebound of recent years? This week will be telling. … And: A look at the AI apps office workers have embraced.

China: Tussling with Trump's Tariffs. The trade war between the US and China continues to heat up as Trump 2.0 approaches its second month and the US merchandise trade deficit hits record levels (*Fig. 1*). Placing tariffs on goods from China and other countries is part of Trump's efforts to boost US manufacturing, level the global trading field, and raise revenues to pay for the tax cuts he plans to extend. The tariffs are also aimed at increasing national security by securing the border with Canada and Mexico against illegal immigration and drugs.

Until 2019, the US imported more goods from China than any other country. Now US imports from China ($444.9 billion, 12-month sum) account for about 13.5% of total US imports, trailing imports from the EU ($605.8 billion) and Mexico ($505.9 billion) (*Fig. 2*). Some Chinese manufacturers have relocated to Mexico and other nations to dodge tariffs, but plenty still ship directly to the US. While off its highs, the US merchandise trade deficit with China remains extremely large at $273.5 billion, using a 12-month sum (*Fig. 3*).

Let's take a look at Trump 2.0's recently announced trade policies and China's responses:

(1) *Trump wastes little time.* Less than a month into the job, President Trump has imposed an additional 10% across-the-board tariff on goods imported from China, reportedly to

encourage China to do more to stop the flow of fentanyl into America. His actions elevate the US tariff rate on Chinese goods above the tariff rate that China imposes on foreign goods: 7.5% using a simple average and 3.0% using a time-weighted average (*Fig. 4*).

President Trump initially canceled the de minimis trade exemption allowing duty-free importing of goods valued at less than $800, which benefits Chinese online retailers like Temu and Shein. But he subsequently reversed that decision, delaying the rule's suspension.

Just this week, Trump announced a 25% tariff on steel and aluminum; but that shouldn't affect Chinese producers much, as only 2% of US steel imports came from China in 2024 (most came from Canada, Brazil, Mexico, and South Korea).

Finally, Trump announced plans to impose "reciprocal" tariffs on a country-by-country basis. In other words, if a country imposes a 10% tariff on American cars sold there, the US will impose at least a 10% tariff on all cars it imports from that country. In setting the tariffs, the US reportedly will also take into account any barriers the country erects to disadvantage US manufacturers, such as value-added taxes on goods made by US companies, government subsidies that tilt the competitive playing field in domestic companies' favor, or regulation preventing US companies from doing business in the country. "[T]he administration could attempt to calculate how much US trade is diverted by foreign trade barriers, and then devise a US tariff rate to reflect that trade volume," a February 11 *WSJ* *article* reported.

(2) *China responds.* China responded to Trump's 10% tariffs on Chinese goods by launching a trade dispute at the World Trade Organization (WTO). The country claims the Trump administration made "unfounded and false allegations" about China's role in the fentanyl trade to justify tariffs on Chinese products. The dispute is expected to have little impact because the WTO's dispute settlement system has been neutered by the Trump and Biden administrations, which blocked the appointment of new judges.

China's response also included a 15% duty on coal and natural gas imports from the US and a 10% duty on US petroleum, agricultural equipment, high-emission vehicles, and pickup trucks. The US tariffs apply to about $450 billion of Chinese goods, while the Chinese tariffs apply to only $15 billion to $20 billion of American goods. In addition, China added tungsten, tellurium, bismuth, molybdenum and indium to its export control list.

China has placed restrictions on US technology companies that could be used as trading cards when negotiating with Trump regarding tariffs. China started an antitrust investigations into Google, which follows an investigation of Nvidia launched last year.

Financials: IPOs Heat Up. The S&P 500 Financials sector is starting 2025 near the top of the ytd performance leader board. Investors hope that some of the sector's largest players will benefit from the Trump administration's business-friendly policies reducing regulation and keeping the capital markets humming along.

Here's the performance derby for the S&P 500 and its 11 sectors ytd through Tuesday's close: Communication Services (7.1%), Financials (6.5), Health Care (6.0), Materials (6.0), Energy (6.0), Consumer Staples (5.2), Industrials (5.1), Utilities (4.7), Real Estate (3.8), S&P 500 (3.2), Consumer Discretionary (-0.1), and Information Technology (-0.5) (*Fig. 5*).

Within the Financials sector, the Investment Banking & Brokerage and the Diversified Banks industries have turned in the strongest performances. Both are helped by the strong stock market and the anticipation of healthy capital markets activity including mergers and acquisitions.

This week will provide clues as to whether the largely moribund IPO market can return to life. Seven deals are scheduled to price this week, including a $1.1 billion offering from SailPoint, an enterprise security firm that secures digital identities.

The following is the ytd performance derby for the S&P 500 Financials sector's industry indexes through Tuesday's close: Investment Banking & Brokerage (11.3%), Diversified Banks (11.3), Insurance Brokers (8.0), Consumer Finance (6.8), Regional Banks (6.7), Financials Sector (6.5), Financial Exchanges & Data (6.1), Asset Management & Custody Banks (-1.3), and Reinsurance (-7.4) (*Fig. 6*).

Here's a look at some of the week's upcoming IPO deals and a few launched earlier this year:

(1) *Improving IPO market.* After an extremely strong market in 2021, when 397 IPOs priced, IPO issuance activity fell off a cliff, with only 71 deals pricing the next year, according to *data* from Renaissance Capital. Activity has slowly been improving in the subsequent years—108 deals in 2023 and 150 in 2024—and the initial 2025 pace looks promising (*Fig. 7*).

So far, 24 deals have priced this year through Tuesday, up 26.3% over same period last year; but the proceeds were only $4.4 billion, down 23.6% y/y. That said, 31 IPO deals have been filed with the Securities and Exchange Commission ytd, marking a 19.2% y/y improvement. And the deals that have come to market are performing well. The Renaissance IPO ETF has climbed 6.0% ytd through Tuesday's close, besting the S&P 500's 3.2% performance over the same period.

(2) *A big test.* The pricing and performance of SailPoint's $1.1 billion IPO will be the latest indicator of whether the market can continue its recovery. In a positive sign, the price range of the shares being offered was increased to $21-$23 from $19-$21 originally.

(3) *Health care IPOs faring well.* Some of the best performing IPOs so far this year are in the health care industry.

Medical device manufacturer Beta Bionics has developed the iLet Bionic Pancreas, an insulin delivery device cleared by the Food and Drug Administration that autonomously determines insulin doses without requiring a user to count carbohydrate intake. The $204 million offering, which priced on January 29, has traded up 32.7%.

Biotechnology company Metsera is developing injectable and oral nutrient stimulated hormone analog peptides to treat obesity and related conditions. The company is in the midst of a phase 1/2 trial for its injectable, with results expected midyear. The $275 million IPO was priced at $18 a share, above its initial $15-$17 range, and it has since traded up by 70.9%.

Another biotech company, Sionna, is developing a treatment for cystic fibrosis that is in phase 1 trials. Shares of the $191 million IPO have traded up 13.4% since coming to market.

(4) *Industry numbers.* Both the S&P 500 Investment Banking & Brokerage and the Diversified Banks stock price indexes are at record highs (*Fig. 8* and *Fig. 9*).

The Investment Banking & Brokerage industry's forward operating earnings per share has broken out to a recent new high and is approaching levels last seen before the 2008 financial crisis (*Fig. 10*). The industry is expected to grow operating earnings by 14.8% this year and 13.2% in 2026 (*Fig. 11*). Diversified Banks' forward operating earnings per share is at a new record high (*Fig. 12*). Its earnings growth is expected to rebound from 3.9% this year to 13.6% in 2026 (*Fig. 13*).

However, both industries' forward P/Es are extended relative to historical levels: 15.4 for

Investment Banking & Brokerage and 13.1 for Diversified Banks (*Fig. 14* and *Fig. 15*).

Disruptive Technologies: AI Loved by the Masses. We've been writing about large language models (LLMs) since early 2023, shortly after ChatGPT made its historic splash. It's been interesting to watch AI gain acceptance. First, just techies were excited about what AI could offer. Then kids started using it to cheat on their homework. Now, recognition of AI's capabilities is on everyone's radar and experimentation with AI has gone mainstream.

Last weekend, Jackie and a group of fifty-something friends discussed how they were using AI at work. One was experimenting with an AI program that turns textbooks or long passages into podcasts. Another uses it to respond to her emails more quickly and to help format Excel spreadsheets. A teacher uses AI to produce lesson plans. None of these folks are techies, but each was excited about using AI to save time at work.

Here's our latest look at some of the popular and novel ways that AI programs are being used at the office:

(1) *The AI podcast.* Google's *NotebookLM* will summarize and make connections between materials that a user uploads. The materials may be a long book, academic pdfs, websites, videos, or all of the above. But what makes NotebookLM eye-popping is its Audio Overview feature, which presents the uploaded material in a conversational podcast format, hosted by two "people." Teachers are using it as a way to reinforce lessons. Students, however, may consider it to be a more entertaining version of Cliff Notes.

(2) *AI monitors customer feedback.* *Frame AI* analyzes customers' calls, chats, surveys, and emails to alert companies to risks or opportunities they might otherwise miss. According to the company's website, Frame AI can use unstructured data to glean insights about what customers want and ways they might use a product. Customer testimonials on Frame AI's website said the AI program allowed them to respond more quickly to customers, anticipate their needs, and improve both customer experience and efficiency.

(3) *AI sees if you're sleeping.* *Read AI* can do all the things you'd expect AI can do with a meeting, like providing a transcript and a summary. What caught our attention is its ability to measure the engagement of those attending online meetings by using AI, natural language processing, and computer vision technology. Read AI measures meeting attendees' verbal and non-verbal cues and translates that into real-time and post-meeting sentiment and engagement metrics. It can also apply AI to past meetings to give presenters coaching metrics and recommendations to help them become better speakers.

(4) *AI at school.* Magic School and Google's Gemini are the AI apps used to save time by our schoolteacher friend. *Magic School* can generate lesson plans, worksheets, rubrics, quizzes, academic content, report-card comments as well as questions, summaries, or presentations based on YouTube videos or a text. Gemini offers many of the same functions. They both make tedious tasks simpler and faster to accomplish.

(5) *Lots of overlap.* Lots of AI apps aim to do roughly the same things, and not all are likely to survive. For example, many AI apps do voice-to-text translation, and many read text out loud. Multiple apps create pictures, edit photos, turn data into charts, help with grammar and schoolwork, and of course answer questions. We wish AI could help us determine which of them will survive and which will go the way of Pets.com.

Calendars

US: Thurs: Headline & Core PPI 0.3%m/m, 0.3%m/m; Initial Claims 216k; Fed Balance Sheet. **Fri:** Retail Sales Total, Ex Autos, & Control Group -0.1%, 0.3%, 0.3%; Industrial Production Headline & Manufacturing 0.3% & 0.1%; Capacity Utilization 77.7%; Business Inventories 0.0%; Import & Export Prices 0.4% & 0.3%. (FXStreet estimates)

Global: Thurs: Eurozone Industrial Production -0.6%m/m, -3.1%y/y; Germany CPI -0.2%m/m, 2.3%y/y; UK GDP 0.1%m/m, -0.1%q/q, 1.1%y/y; UK Headline & Manufacturing Industrial Production 0.3% & 0.0%m/m, -2.0% & -1.8%y/y; ECB Economic Bulletin; European Commission Winter Forecasts; Nagel; Cipollone. **Fri:** Eurozone GDP 0.0%q/q, 3.0%y/y; Eurozone Employment Change 0.1%m/m, -0.1%q/q, 1.1%y/y; Germany CPI -0.2%m/m, 2.3%y/y; UK Headline & Manufacturing Industrial Production 0.2% & -0.1%; UK GDP -0.1%m/m. (FXStreet estimates)

Strategy Indicators

S&P 500 Earnings, Revenues, Valuation & Margins (*link*): The S&P 500's forward revenues rose 0.5% w/w during the February 6 week to its first record high since the January 9 week. Forward earnings also rose 0.5% w/w to a new record high. The forward profit margin remained steady w/w at a record high of 13.6%. It is now 3.3ppts above its seven-year low of 10.3% during April 2020. The consensus expectations for forward revenues growth dropped 0.1ppt w/w to 5.5%, and is now 0.3ppt below its 23-month high of

5.8% during the August 1 week. It has gained 3.2ppts from its 33-month low of 2.3% during the February 23, 2023 week. That's down from a record high of 9.6% growth at the end of May 2021 and compares to 0.2% forward revenues growth during April 2020, which was the lowest reading since June 2009. The forward earnings growth forecast tumbled 1.2ppts w/w to a 36-week low of 12.6%, and is now 1.7ppts below its 38-month high of 14.3% during the December 12 week and 9.3ppts above its 31-month low of 3.3% during the February 16, 2023 week. That's down from its 23.9% reading at the end of April 2021, which was boosted by the recovery from the pandemic to its highest reading since June 2010 and up substantially from its record low of -5.6% at the end of April 2020. Analysts expect revenues to rise 5.3% in 2025 (down 0.1ppt w/w) and 6.3% in 2026 (unchanged w/w), an acceleration from 2024's forecasted 4.9% (up 0.2ppt w/w). They expect an earnings gain of 12.2% in 2025 (down 1.5ppt2 w/w) and a 14.1% rise in 2025 (up 0.1ppt w/w) compared to 2024's forecasted earnings gain of 11.1% (up 0.8ppt w/w). Analysts expect the profit margin to rise 0.8ppt y/y to 13.3% in 2025 (down 0.1ppt w/w) and 1.0ppt y/y in 2026 to 14.3% (down 0.1ppt w/w), compared to 2024's forecasted 12.5% (up 0.1ppt w/w). The S&P 500's weekly reading of its forward P/E ticked down 0.1pt w/w to 22.0, and is just 0.4pt below its 43-month high of 22.4 during the December 12 week. It's up 2.3pts from a 14-week low of 19.7 during the August 8 week and 6.7pts from a 30-month low of 15.3 in October of 2022. It also compares to 23.1 in early September 2020, which was the highest level since July 2000, and to a 77-month low of 14.0 in March 2020. The S&P 500 weekly price-to-sales ratio was steady w/w at 2.99 and remains just 0.03pt below its December 12 record high. That's up from a six-month low of 2.22 during the October 26, 2023 week and compares to a 49-month low of 1.65 in March 2020.

S&P 500 Sectors Earnings, Revenues, Valuation & Margins (*link*): During the February 6 week, forward revenues rose for ten of the 11 S&P 500 sectors and forward earnings rose for seven. This led to rising forward profit margins for four of the 11 sectors. These seven sectors posted record-high forward revenues this week: Communication Services, Consumer Discretionary, Consumer Staples, Health Care, Information Technology, and Real Estate. Industrials' forward revenues has weakened to 3.2% below its early September record. Materials and Energy are improving again after stalling repeatedly, but they remain the biggest laggards at 5.8% and 15.5% below, respectively. These five sectors had record-high forward earnings this week: Communication Services, Consumer Discretionary, Financials, Information Technology, and Utilities. Consumer Staples has dropped to 0.6% below its record high in early January. Improving now is Real Estate at 1.5% below its record high in August 2022 and Health Care at just 0.5% below its February 2022 record. Among the remaining two sectors, forward earnings remains depressed for Energy and Materials, which are 34.2% and 25.7% below their respective highs during 2022. Looking at the record-high forward profit margin club, Financials' was steady w/w after entering the club during the January 16 week for the first time since August 2021. Also at a record high this week is Communication Services. In recent weeks, the Consumer Discretionary, Industrials, and Information Technology sectors were in that club. Among the laggards, Energy's forward margin fell 0.1ppt w/w to 9.4%, just 0.1pt from its 34-month low of 9.3% in late December and has tumbled 1.5ppts since its six-month high of 10.9% in mid-June; Consumer Staples' 6.8% is just 0.1ppt above its seven-year low in March 2023; Health Care's 8.6% is only 0.1ppt above its record low in April; and Real Estate's 16.9% is up from a low of 12.4% in December 2020. Here's how the S&P 500 and its 11 sectors rank based on their current forward profit margin forecasts along with their record highs: Information Technology (27.0%, down from its 27.6% record high in September prior to low-margin Dell's index addition, which lowered the margin 1.3ppts then to 26.3%), Financials (20.0, a record high for a fourth week, the first since August 2021), Communication Services (18.6, a record high this week), Real Estate (16.9, down from its 19.2 record high in 2016), Utilities (14.5, up 0.1ppt w/w and down from its 14.8 record high in April 2021), S&P 500 (13.6, a record high this week and in 22 of the past 23 weeks), Materials (10.6, down 0.2ppt w/w to a 12-month low and from a 20-month high of 11.6 in July 2023 and a 13.6 record high in June 2022), Energy (9.4, down 0.1ppt w/w to just 0.1ppt above its 34-month low of 9.3 in late December and down from its 12.8 record high in November 2022), Industrials (11.2, down from its 11.3 record high in early January), Consumer Discretionary (9.4, up 0.1ppt to a record high this week), Health Care (8.6, only 0.1ppt above its 8.5 record low at the end of April and down from its 11.5 record high in February 2022), and Consumer Staples (6.8, down from its 7.7 record high in June 2020).

US Economic Indicators

CPI (*link*): Both the headline and core CPIs in January were a surprise on the upside. *Headline* CPI rose 0.5% (vs 0.3% expected)—the largest monthly gain since August 2023, while the *core* CPI increased 0.4%, double December's 0.2% gain and the largest monthly increase since April 2023. On a *year-over-year basis,* the headline rate climbed to 3.0%, up from September's 2.4%—which was the lowest rate since February 2021; it peaked at 9.1% in June 2022. Meanwhile, the core rate was at 3.3% in December, for the fifth time in six months, after slowing from September 2022's 6.6% to 3.2% in July of last year—which was a three-year low. The *goods inflation* rate rose to 0.8% y/y in January after falling -1.3% in September, with the durable goods rate at -1.2 y/y, narrowing from August's -4.2%; the rate peaked at 18.7% in February 2022. The rate for nondurable goods (1.6% y/y) moved above zero for the first time in four months in November and has accelerated steadily from a recent low of -0.7% in September; it peaked at 16.2% in June 2022. *Services excluding energy services* is drifting lower, though remains relatively high at 4.3%, well above rates a couple of years ago. Looking at *durable goods prices*, major appliances (-4.2% y/y), furniture & bedding (-2.6), and new vehicles (-0.3) are still falling, though the rate for the latter is nearing zero. Meanwhile, the rate for motor vehicle parts & equipment moved back above zero in August and remains in a relative flat trend just above 1%. Here's a snapshot of yearly rates for some key *nondurable goods* prices from highest to lowest: recreational commodities (8.0%), food (2.5), medical care commodities (2.3), housekeeping supplies (0.9), and apparel (0.4). The rate for recreational commodities is down from its recent high of 11.2% in April, while energy prices fell back below zero in August (-4.0) and fell deeper into negative territory in September (-6.8), though the decline narrowed to -3.2 by November and moved above zero in January (1.0%) for the first time in six months. It posted a recent peak of 3.7% last May. The rate for medical care commodities drifted down toward zero from its recent peak of 3.1% in June. Turning to services inflation, *rent of shelter* remains high, though the yearly rates are easing from their recent highs in April 2023: rent of primary residence (to 4.2% from 8.8%) and owners' equivalent rent (4.6 from 8.1). Turning to *non-housing-related services*, the yearly rate for transportation service (8.0) remains high, though is down from recent highs, while the rate for recreation services (3.8) is up from September's 2.2%—which was the lowest since mid-2021. Meanwhile, the yearly rate for education & communication services is hovering just below 2.0%, while the medical services (2.7) is up from its recent bottom of -2.6% in September 2023, though has eased in recent months. The rate for other personal services (2.3) has dropped to its lowest since February 2021.

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