The Economist

Hard truths about manufacturing

Delivery drones and flying cars

Ecuador's gang-busting

Europe's defence cities

JUNE 14TH-20TH 2025

American disorder

Business

Photograph: Getty Images

America and China reached a tentative agreement on trade following talks in London that were attended by senior members of both governments. America's main sticking-point was greater access to China's rare earths, which the White House said had been resolved. Under the framework America will still charge a 55% tariff on Chinese goods, made up of a 10% reciprocal levy, 20% tariff related to fentanyl smuggling and 25% in existing duties. Donald Trump described it as a done deal, which would include Chinese students "using our colleges and universities".

Chart: The Economist

Constrained by Mr Trump's trade war, China's exports to America plunged by 35% in May, year on year. Many businesses brought forward their orders for Chinese goods earlier in the year to beat the imposition of tariffs. Still, China's exports in total increased by 5% in May, and were up by 12% to the European Union.

Despite Washington's newfound bonhomie with China over trade, the United States embassy in Panama announced that the American government would replace telecoms towers in the country that have been made by Huawei, a Chinese company, with "secure American technology". This would help "counter the malign influence of China throughout our hemisphere", it said.

The World Bank cut its estimate of global growth this year because of "trade-related headwinds". The world economy is now expected to expand by 2.3%, down from the bank's January forecast of 2.7%. America's GDP is now expected to grow by 1.4%, down from 2.3% in January. The bank said that "Without a swift course correction, the harm to living standards could be deep".

Central banks worldwide now hold almost as much gold as they did in 1965, according to the European Central Bank, which found that bullion had replaced the euro in 2024 as the second-biggest store of official reserves, after the dollar. Gold prices have rocketed from $2,320 a troy ounce a year ago to around $3,350.

A stitch-up?

In France the Senate voted for a bill to ban advertising for fast-fashion companies such as Shein and Temu amid concerns that their cheap almost-disposable clothing is not environmentally sustainable. The bill has a whiff of protectionism about it by making a distinction between "ultra" fast fashion, such as that sold by the two Chinese companies, and "classic" fast fashion supplied by European retailers, such as Zara and H&M.

Following Mr Trump's imposition of tariffs on cars made in Mexico, General Motors announced plans to invest $4bn in its factories in the United States, bringing home the production of some vehicles that currently takes place across the border.

America's annual rate of inflation rose slightly in May, to 2.4%. There is little evidence so far that the higher costs of imported goods, because of tariffs, are being passed on to consumers, though economists expect that to change in the coming months.

The British government confirmed that it would invest a further £11.5bn ($15.5bn) in the Sizewell C nuclear plant on top of the £2.7bn it put in last year. The plant is expected to start supplying energy to homes in the mid-2030s, but the funding commitment is only for the current parliament, or around three to four years.

Warner Bros Discovery decided to split into two separate companies, one focused on its film studio, HBO and streaming assets and the other on its television channels, which include CNN. The split frees the fast-growing streaming side of the business from the waning cable-TV side.

Apple's annual Worldwide Developers Conference was an unusually subdued affair. The main announcements were an upgrade to Apple's operating system and a decision to let app developers access its artificial intelligence, but there were no big developments in AI. Apple is reportedly struggling to create the large language models it needs and investors are worried that it is falling behind in the AI race. Its share price has fallen by more than 20% this year, an even worse performance than Tesla's.

When bros become foes

Tesla's stock clawed most of its losses, after falling by 14% when Mr Trump threatened to end government contracts with Elon Musk's companies following the spectacular break-up of their relationship. Mr Musk has left the government and criticised Mr Trump's "big, beautiful" spending bill. "I regret some of my posts" about the president, he said, without elaborating if that meant his claim (for which he produced no evidence) that Mr Trump is mentioned in secret files on Jeffrey Epstein, a deceased sex offender. Mr Trump said he had "no hard feelings" and opened the door to a reconciliation.

Finance & economics

European stocks are buoyant. Firms still refuse to list there

Our estimate of their impact will update every month

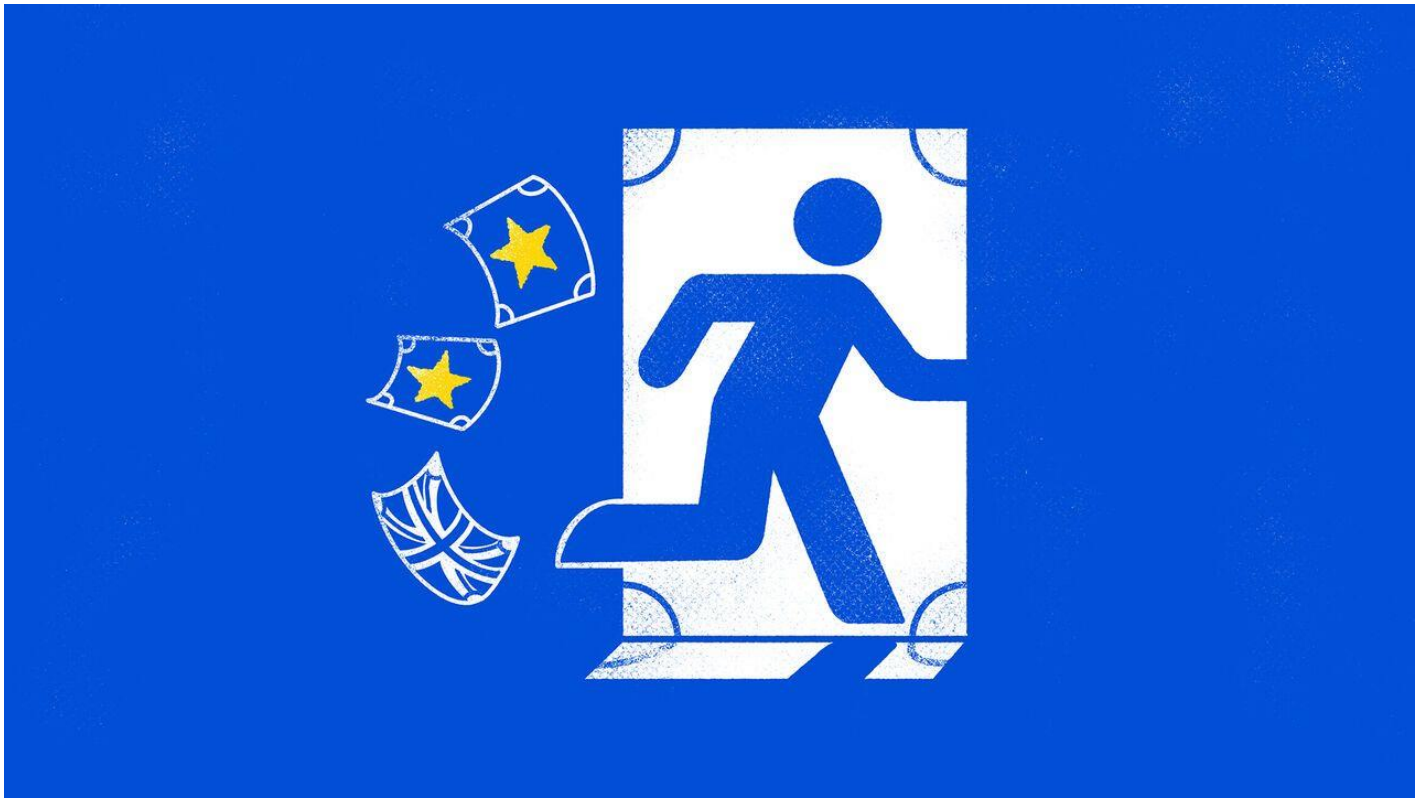

Illustration: Satoshi Kambayashi

It must be tempting to give up. Those tasked with reviving Britain's stockmarket have long faced a difficult task and a steady drip of bad news, as one firm after another departs for private ownership or America. It will still have hit like a bucket of cold water to learn, on June 5th, that Wise intends to move its main listing to New York.

One of Europe's hottest fintech outfits, Wise's flotation in London in 2021 spurred hopes that other stars would follow. If they included Klarna and Revolut, two even hotter peers, the London Stock Exchange would add a new, buzzy cluster to its old-timers in banking, energy and mining. That would attract attention from stock analysts, capital from international investors and yet more listings. Four

years on, it has not worked out. Like Wise, Klarna intends to float in America; Revolut's boss has hinted that it may do so, too.

The failure to attract and retain fast-growing firms is most often laid at the doors of the London Stock Exchange, but it is a pan-European malaise. Klarna, after all, is Swedish. So is Spotify, the only European firm founded this century worth more than $100bn. It listed in New York in 2018. New Financial, a think-tank, reckons that in the decade to 2024 some 130 companies moved their listing from Europe to America, while over 1,000 were taken private. In today's money, their total value at the point of de-listing adds up to $1.7trn—more than 10% of what Europe's stockmarkets are worth. Proportional to market capitalisation, Ireland is the biggest loser, followed by Sweden, Britain and Germany.

Unnerved, Europe's financial elite has responded in time-honoured fashion: it has convened task-forces, launched consultations and commissioned reviews from grandees that, if printed, would fell forests. There have been extravagant promises of streamlined reporting, harmonised regulations and centralised supervision. In what may eventually be a radical step, Britain's government is mulling plans to force some retirement savings to be invested at home.

It is, in fact, unfair to make fun of these efforts. Speak to bosses of private firms in Europe, or to their investors, and they will commend these incremental reforms to make the continent's stockmarkets work better. A European listing, they will say, might make sense for plenty of companies. Then, without missing a beat, they will explain why theirs is not one of them and America is a better fit.

Frequently, most of the company's shareholders will be American already. "They would find it weird if I didn't list there," says the boss of a European startup planning its initial public offering. Listing in America means using bankers and a wider milieu with which the investors are already familiar. More importantly, if the company has global ambitions, which pretty much all those backed by venture capital do, America's consumer market is among the most lucrative. An IPO in New York might build the brand. It does not hurt that the median boss of a firm in America's S&P 500 share index is paid two and a half times their equivalent in Britain's FTSE 100. The biggest and most consistent bugbear among tech founders is that nervous European investors are perennially reluctant to approve the high-risk, high-growth strategies that they want to pursue.

Just as important are the factors that startup bosses do not mention. The main one is the supposed "valuation gap", meaning the higher average multiple by which earnings are scaled up to generate share prices for firms listed in America as opposed to Europe. Perhaps sensing that harmonised regulation does not set pulses racing, proponents of Europe's exchanges have recently switched tack,

reasonably arguing that the valuation gap is a myth. Control for expected profit growth and the different markets' sectoral mixes, and it disappears.

Before Arm, a British chip designer, listed in New York in 2023, the City of London was rife with rumours that the perceived valuation gap was why the local stock exchange missed out. But the gap does not seem to be behind recent moves. Wise's chief financial officer has said that valuation was "not really the driver" of his firm's decision. This makes sense: at 29 times its expected earnings for the coming year, it is already more richly valued than the S&P 500 average. Meanwhile, European shares have recently been outperforming American ones. The most disheartening thing for those trying to patch up Europe's capital markets is that the companies they must woo are simply not interested.

How to invest your enormous inheritance

Do not make the mistakes of the first Gilded Age

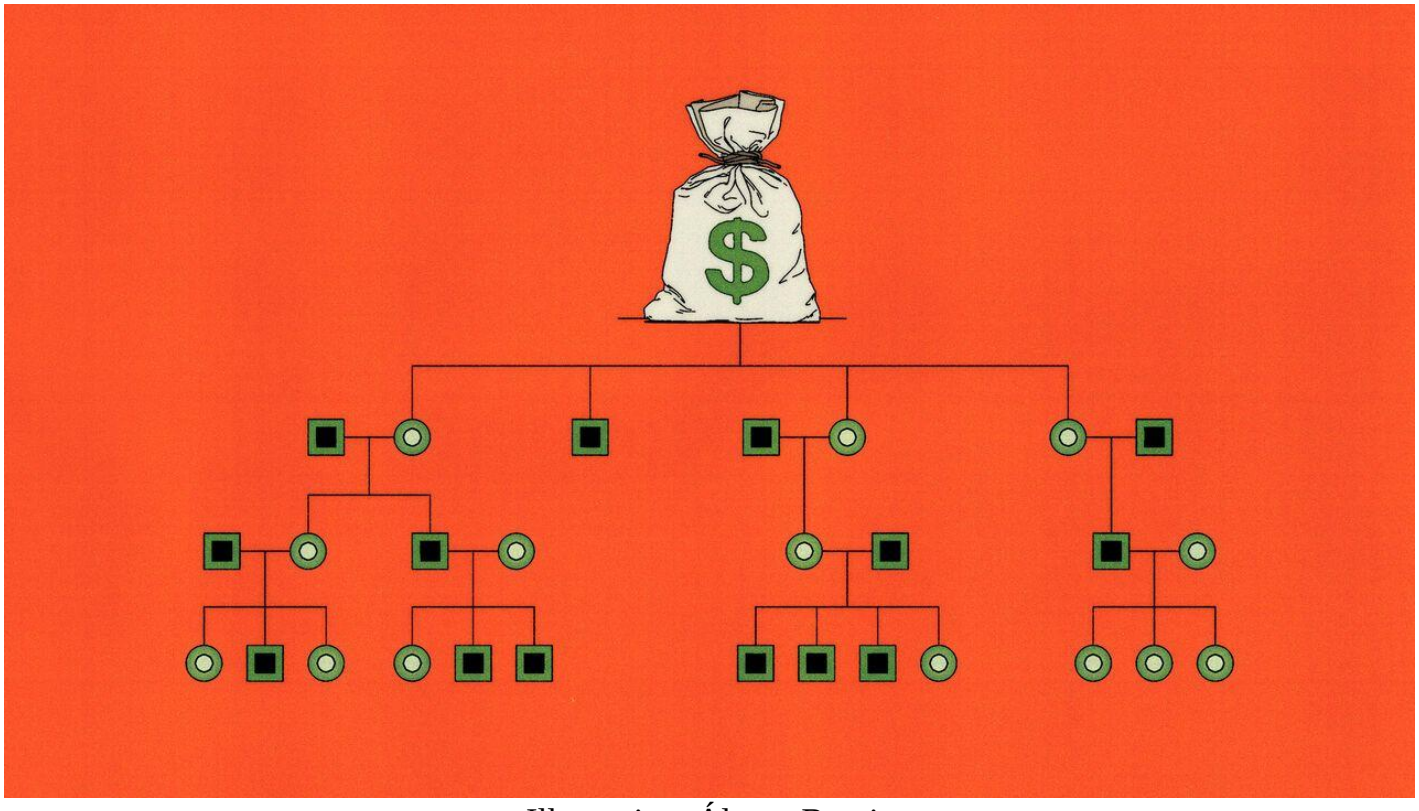

Illustration: Álvaro Bernis

What do you stand to inherit? It still feels like a question from a different age, despite its growing importance today. In 2025 people across the rich world will inherit some $6trn, or around 10% of GDP—a figure that has climbed sharply in recent decades. French bequests have doubled as a share of national output since the 1960s; those in Germany have tripled since the 1970s; Italian inheritances are now worth around 20% of GDP (see chart 1).

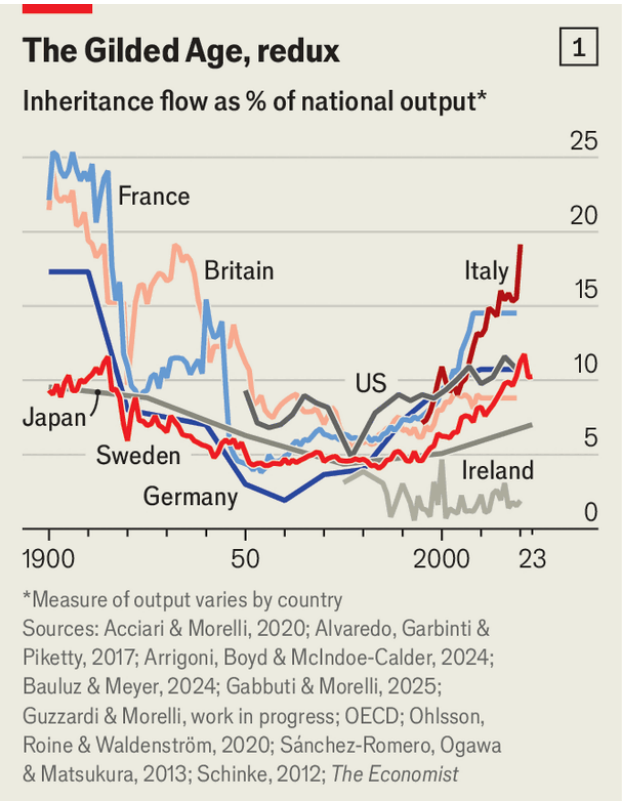

Chart: The Economist

There are two entirely reasonable responses to this. One is to worry about the new inheritocracy harming society: how it could corrode incentives to work, say, or widen inequality and distort the marriage market. The other, if a windfall is coming your way, is to rub your hands in glee and ponder what you ought to do with it.

The typical inheritance is closer to the value of a typical home than to a Vanderbilt-style fortune. Even so, a rising number of people are in line for a bonanza. UBS, a bank, reckons that 53 people became billionaires in 2023 by inheriting money; many more will have received amounts in the hundreds of millions. Asset prices have climbed so high in recent decades, and inheritance taxes have fallen so low, that the number of very wealthy scions is growing all the time. Descend from the stratosphere, and a sizeable cohort is set to receive far

lower sums that will nevertheless be life-changing. In Britain, for instance, a quarter of 35- to 45-year-olds are expected to inherit more than £280,000 ($380,000).

For these lucky people, the experience of the Vanderbilts and their contemporaries offers a cautionary tale. At the turn of the 20th century, America's census recorded about 4,000 millionaires, note Victor Haghani and James White, two wealth managers, in their book, "The Missing Billionaires". Suppose a quarter of them had at least $5m (the richest had hundreds) and had invested it in America's stockmarket. Had they then procreated at the average rate, paid their taxes and spent 2% of their capital each year, their descendants today would include nearly 16,000 old-money billionaires. In reality, it is a struggle to find a single one who traces their fortune back to the first Gilded Age.

That is not down to inflation or the 20th century's wars, but to poor investment and spending decisions. After all, spending 2% of $5m in 1900—that is, $3.8m in today's money—would not exactly have consigned anyone to penury. The big question for a 21st-century heir is how to avoid the mistakes of those of the past. In other words, how can you enjoy a nice life while ensuring your inheritance lasts for ever?

Silver spoons for all

Some cheery news is that the question of how to invest, which sounds like the hardest part, need not be solved perfectly. In theory, this would mean finding the blend of risky assets with the best volatility-adjusted return, and comparing it with the "safe" return on inflation-protected government bonds. You would then solve for an optimal split between the two, which would vary with market conditions.

Thankfully, far simpler procedures can produce spectacular results. Our putative 20th-century millionaires just plonked everything in America's stockmarket, and did very well. Today, we know they could have done even better without much more effort. A simple rule-of-thumb known as the "Merton share" can approximate the optimal split between stocks and inflation-protected government bonds, by comparing their expected returns and volatility.

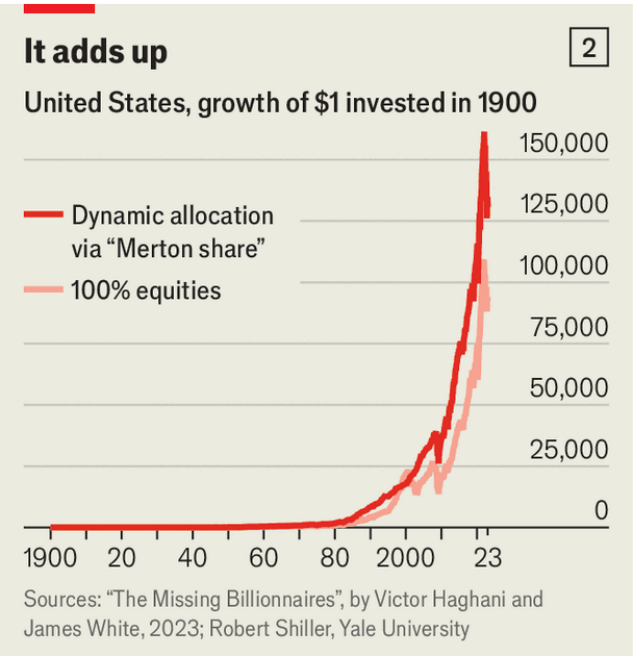

Chart: The Economist

Messrs Haghani and White have calculated the annualised returns on such a strategy since 1900 (using a proxy for inflation-linked bonds for before 1997, when they were first issued). The results are shown in chart 2. Had the Gilded Age crowd and their descendants invested in this manner, they would have scored an annualised nominal return of 10%, compared with 9.8% from the all-stock strategy. Remarkably, it would also have been 30% less volatile. That would have produced vastly more old-money billionaires today.

The worse news is that deciding how much to spend is trickier than it sounds. Popular rules for drawing down retirement savings, such as spending a largish fixed percentage of the initial value each year, are definitely out. In truth, these are not wise even for pensioners. Suppose you had kept a classic 60/40 split between American stocks and government bonds, starting in 2000, and drawn down 5% of the value of your initial savings a year. You would have run out of money in 2019, despite earning an annualised return of 5.25%, since you would have depleted too much capital in the market's "down" years.

Even if you spent only 4% of the initial value each year—well below the portfolio's return—you would run a high risk of going bust. Simulate many different market outcomes, based on the 60/40 portfolio's expected return and volatility, and the 4% spending rule leads to ruin within three decades about a third of the time.

To avoid this trap, the optimal amount to spend each year must be a percentage of the portfolio's value at that point (the "spending ratio"), not of its initial value. In other words, if you want to take the risk required to generate outsize returns, you must vary your (maximum) spending from year to year. That way, after a bad spell for the markets, you will not deplete too much of the remaining pot, allowing it to recover. Each year you could, for example, spend a proportion of the portfolio's value equal to its annualised expected return. This is similar to the spending rule adopted by university endowments, which aim to solve the same problem. The median outcome is that the fund's value, and hence annual spending, stays roughly constant with time (provided you have not been overly optimistic about your returns).

Nice—but hardly enough to start a dynasty. Ideally, you want to increase your portfolio's value, which means spending less to let the returns rack up. The trade-offs here are difficult to parse. You will get pleasure (or, in economists' jargon, "utility") from spending more today, albeit with diminishing marginal returns as you get more and more profligate. Doing so will also trim your descendants' purchasing power, especially if the portfolio has a large expected return, which you in part forgo by spending now. Yet such returns are inherently uncertain. In any case, it is only human to prefer an immediate pay-off to a delayed one ("time preference").

The solution is to plug these dynamics into a mathematical model, simulate possible paths for financial markets and calculate the utility derived from each for a given level of spending. You can then calculate the expected utility for each rule and pick the one that maximises this. Unsurprisingly, the procedure is hard, and generates results that are sensitive to the inputs. Maybe spend some of your money on an excellent financial adviser.

Yet there are straightforward lessons that everyone can absorb. Although greater expected returns allow you to spend more, they do not do so by as much as you might think. With higher returns, the gap between these and the optimal spending ratio widens (since there is more value in sacrificing spending to let the portfolio grow). Higher volatility means lower spending, since it drags on your annualised return. The more reluctant you are to vary year-to-year outlays, the less you can tolerate investing in stocks, since their value fluctuates. The smaller your minimum spending requirement, the more risk you can take, meaning your expected returns, and hence your overall spending, can rise.

A more important lesson is that making your inheritance last for ever means spending far less than its expected return. Exactly how much less depends on market conditions and your risk and time preference. But under reasonable assumptions, a near-optimal portfolio might have

an expected annualised return of 4.1% and an optimal pre-tax spending ratio of 2.4% per year. Even that is before allowing for how much your family tree might grow, cutting whatever you pass on into smaller chunks. “People often want to know how much they need to have to give each member of their family’s next few generations a modest income,” says Mr Haghani. “The answer is: a lot more than most anyone thinks.

The economic lessons from Ukraine’s spectacular drone success

National security is a weak argument for battery subsidies

Illustration: Álvaro Bernis

On June 1st Ukraine took military raiding into the 21st century. It did so with little more than ingenuity and 117 drones, which emerged from trucks across Russia—everywhere from Siberia to the Chinese border—and destroyed a dozen or so planes in Vladimir Putin’s long-range air fleet. The raid came amid the Russian

president's relentless bombardment of Ukraine. On June 9th he launched his biggest drone strike of the war, sending 479 machines to hit Ukrainian airfields, cities and factories.

As many as half of casualties on the front line are inflicted by drones, according to a Ukrainian doctor. The "Spider's Web" operation was a demonstration of the machines' supreme importance. For the West, it was also a reminder that an important military technology is dominated by an adversary, namely China, which supplies batteries and motors used by both sides. That raises a question. If, say, a conflict over Taiwan were to escalate, could America and its allies step up production fast enough?

Many people believe that a country with a vibrant electric-vehicle industry has a decisive advantage in the manufacture of drones. Lots of the batteries for EVs use lithium-ion technology; so, too, do most shorter-range drones. And in the race for battery supremacy there is only one winner: China, which accounts for 85% of global EV capacity. The European Union is studying whether this dominance would put China ahead in the event of a conflict; American officials are under pressure from companies and think-tanks to dole out subsidies to ensure that the country wins any "battery war". If subsidising battery production is such a good idea, then President Donald Trump's budget bill, which promises to end all EV subsidies, is a hugely damaging policy.

America has sought an EV industry to rival China's since 2009, when the Obama administration first subsidised consumer purchases. Joseph Shapiro of the University of California, Berkeley, and Hunt Allcott of Stanford University estimate that, in 2023, each additional EV sold owing to subsidies cost the government $32,000. Supporters of such an approach see this as sensible not just on environmental grounds, but on national-security ones. The batteries produced by a healthy EV industry could, in the event of a conflict, be repurposed to fuel drones.

Consider the mechanics of warfare in Ukraine, however, and the argument becomes less compelling. Ukraine's drones range from small, autonomous boats patrolling the Black Sea to aircraft that travel hundreds of kilometres into Russia. Most are designed to be made from parts that are cheap, easy to find and simple to put together, according to a firm a few miles outside Kyiv, which builds them in an airy suburban home. Another firm, established two years ago and now making some of Ukraine's most sophisticated drones, locates its production line in a series of garages, so as to minimise disruption from Russian airstrikes.

Most Ukrainian drones are single-use, short-range "kamikaze" ones that travel just a few kilometres before blowing themselves up—more akin to munitions than aircraft. The batteries of some store a mere 77 watt-hours of energy, compared with the 20,000-100,000Wh common in EVs. Meanwhile, production lines have become less flexible owing to the high-tech nature of modern EV-making. "It is unimaginable...that a Tesla factory would be anywhere near as useful for production as a Detroit factory was in the second world war," says the boss of a defence firm.

China has grown closer to Russia, so Ukrainian drone producers have found their old Chinese suppliers less keen to do business. Several, including Wild Hornets, now import battery cells from South Korea and assemble

their own packs. Pawell, another firm, is working on its own battery chemistry. Already, building batteries in Ukraine is only a little more expensive than buying them from abroad. Wild Hornets sells its ones for simple drones at $90 a piece. Drone batteries, it turns out, are simpler to make in wartime than an EV industry is to nurture in peacetime.

Indeed, American battery-makers could adjust quickly if required—without the need for assistance from EV-makers. For proof, look at their response to the supercharged subsidies that the Biden administration introduced in 2023. Although America's capacity still lags far behind China's, the country's production has surged from 0.11 terawatt-hours in 2022 to 0.44tWh this year. Include production in Europe and among East Asian allies, and that is already sufficient to furnish Ukraine with kamikaze drones for 3,750 years at the current rate of use.

Drop a bombshell

Were American drone production to be hamstrung in a conflict with China, it would not be by industrial capacity. Ukrainian firms are now discovering that the most pressing shortage is motors, rather than batteries. They need magnetic components containing rare-earth metals that are produced and refined by China. More mineral refining, not manufacturing, is the solution.

Another question is whether America's armed forces would be able to adapt to drone warfare. So far, the Pentagon has been slow to adjust to the pace of drone experimentation and manufacturing demonstrated by Ukraine. The US Army seeks to put 1,000 drones in each of its dozen divisions. The Pentagon's Replicator Initiative, launched by the Biden administration, aims to field "tens of thousands" of AI-enabled drones. Ukraine claims to have produced 1.5m drones last year, and does so at far lower cost, in part because it is less squeamish about using parts from China.

Industrial-policy advocates might like to rescue EVs from Mr Trump's chainsaw. Unfortunately for them, arguments involving national security offer little protection. America does not need a bigger battery industry to master drone warfare. It needs more mining, more refining and more imagination.