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WEEKLY ECONOMIC COMMENTARY

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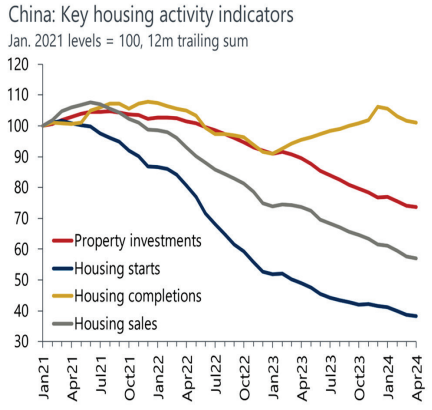
One of the longest nonstop commercial flights in the world is the trip between Los Angeles and Singapore, at just under 18 hours. I found myself on the route three weeks ago; to pass time, I took two long naps, watched three movies, ate two meals, and cleared about 2,000 e-mails.

The journey was tiring, but my energy was restored during two weeks of interesting meetings in Malaysia, Singapore, China, and Hong Kong. Following are my main take-aways from the trip.

- **China is struggling to find the right formula for economic stimulus.**

Official measures of real growth are still aligned with the country's 5% target, but consumer confidence and spending are soft, export growth has slowed, and business investment has slumped. China is experiencing its largest capital outflows in 15 years, and its equity markets are significantly underperforming.

With an outlook that calls for stimulus, monetary policy in China has become more restrictive. Inflation has fallen, and real interest rates have risen. The money supply is growing more slowly than it has at any time in the last 20 years. With a deleveraging trend in place, lowering interest rates will have limited benefit and could place further pressure on the Chinese currency.



Sources: China Ministry of Commerce, Bloomberg, Oxford Economics, ONS

China has announced a program intended to deal with the overhang of apartment inventory. 300 billion yuan (around $40 billion) will be allocated to state-owned enterprises controlled by local governments, which will use the money to purchase unoccupied units and convert them to affordable housing. The program aims to establish a floor on property values and bring supply into better alignment with demand.

But the effort raises a host of questions. It isn't clear how prices will be set; current owners will almost certainly realize a substantial loss. The amount allocated represents less than 5% of China's aggregate residential property value, likely not enough to stabilize values. And many local governments are in severe financial distress, and may not be in the best position to execute the plan.

There was concern about Chinese deflation among many I spoke with in the region. The policy response to date has been piecemeal. The situation seems to call for broad fiscal stimulus, but high levels of public debt have Chinese officials hesitant.

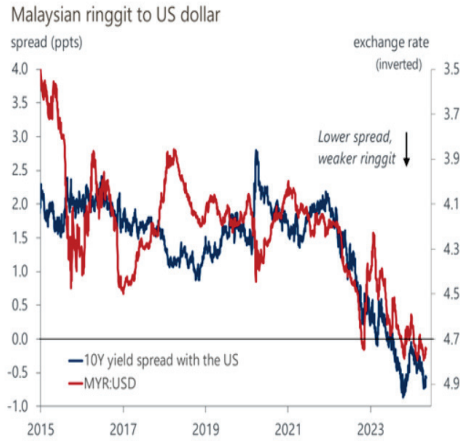
I returned home with more concerns about China.

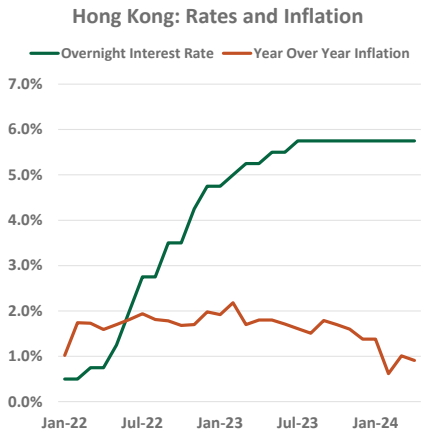
I returned home with a somewhat higher level of concern over China's economic outlook. The implication of underperformance for the region and the world could be significant.

- **Those of us who live in large countries often don't appreciate how hard it is for developing countries to make economic progress.**

One of the more poignant moments of the trip was an address from Malaysia's economic minister at an event we hosted. He spoke articulately about his country's challenges and opportunities, highlighting the need to complement traditional industries with newer ones. He also noted the importance of attracting foreign capital, using the phrase "China plus one" as an invitation for firms to use his country as complement to operations in China.

But internal and global politics can present obstacles. Electorates have limited patience, and managing alignments between East and West is terribly difficult for emerging markets. The minister struck the right balance between realism and idealism, a posture that I would recommend as we consider prospects for emerging markets.





Sources: Oxford Economics, Haver Analytics, Bloomberg

- **Asian central banks are in a difficult position.**

Higher-for-longer interest rates in the United States are causing a great deal of discomfort in the region. Hong Kong provides a case in point: real gross domestic product (GDP) in Hong Kong is still below its 2019 level, and asset values are under pressure. Inflation is less than 1% over the past year, and falling.

But because the Hong Kong dollar is pegged to the U.S. dollar, the Hong Kong Monetary Authority cannot ease until the Fed does. Few countries have this kind of official peg for their currencies, but many have to maintain an informal link to keep capital from leaving the country.

I was asked frequently if the Federal Reserve recognizes the impact its policy has overseas. The Fed is certainly conscious of its global influence, but its Congressional mandate focuses on domestic inflation and employment. Unless stress overseas threatens growth or financial stability in the U.S., the Fed is unlikely to relent.

- **The U.S. election is being closely watched in Asia.**

Many I spoke with expressed frustration that neither of America's political parties seems interested in normalizing economic relations with the region. I was also asked often how U.S. markets and the U.S. dollar can perform so well amid so much political dysfunction. (To be honest, I did not have a great answer to that question.) Our deep budget deficits and the mosh pit that Washington has become diminish the desire of Asian countries to follow the American model.

U.S. policy has a huge influence on Asia's economies.

- **The food culture in Asia is always amazing.**

This year's fare included white pepper crab, Sichuan-style crawfish, and Beijing-style hot pot with lamb. Morning coffee is often strong, over ice, and flavored with just a hint of sweetened condensed milk. That gets the day started right.

Memorably, a group of us escaped the office for lunch one day and went to the Tiong Bahru hawker center in Singapore. We gorged on slow roasted pork belly, freshly made wontons with chili, noodles with roasted duck and kueh with pandan (sweet rice flour cakes). Unfortunately, I was dressed in a suit, which wasn't suitable for the humidity or the occasional chopstick malfunction.

45 hours in the air over two weeks is no one's idea of a good time. But the reward for all of that flying came in the form of memorable meals and conversations. I hope it won't be long before I return.

For Richer Or Poorer

Globalization conjures thoughts of trade in goods, but it has also opened up tremendous flows of capital. The trade balance tends to grab the most attention as it forms part of the gross domestic product (GDP) equation, but foreign investments have a significant effect on recipient nations.

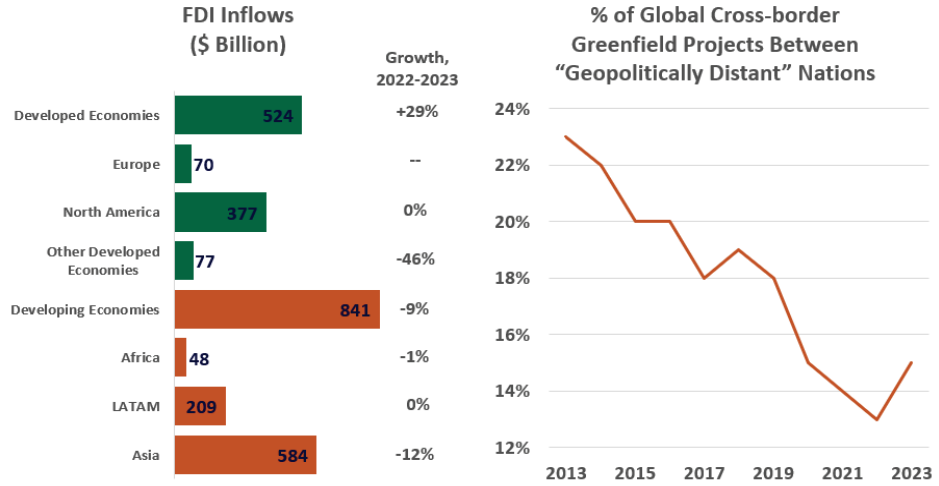
Foreign direct investment (FDI) brings overseas capital into a domestic economy. Providers commit to a lasting presence and act as a catalyst to economic development. It is more of a marriage than a fleeting friendship.

But the landscape for FDI, once a hallmark of globalization, has been changing. Global FDI growth has stagnated since 2010, failing to keep pace with trends in merchandise trade and GDP. The bigger concern is the recent drop in flows to developing countries, given their reliance on foreign investments as a driver of growth.

FDI into emerging markets (EMs) declined 9% to $841 billion in 2023, with falling or stagnating flows across most regions. Major Asian markets witnessed the largest fall of 12% last year. China reported a rare 6% drop in FDI inflows last year. Flows to the Association of Southeast Asian Nations, which were supposed to benefit from reshoring, declined by 16%.

Despite the euphoria surrounding the Indian economy and improving ties with the West, India has also been falling out of favor and struggling to become a "plus one" country as investors diversify away from China. India saw a 47% drop in FDI inflows in 2023. Repatriation and divestment by direct investors has surged.

Higher financing costs partly explain the weaker flows to EMs last year. Easier monetary conditions should support investments in 2025, though high debt burdens will continue to cast a shadow over the global investment landscape.



Source: UNCTAD

Economic considerations are no longer the sole driver of investment decisions.

Geopolitics are another major driver realigning investment decisions and destinations. Increased scrutiny and restrictions on activities are discouraging flows to recipient nations. Investments between geopolitically distant countries – those with divergent political interests or foreign policies – have decreased from 23% in 2013 to 15% in 2023. Research shows that geopolitical tensions between an investing and a recipient country reduce bilateral cross-border portfolio and bank allocations.

Advanced economy governments are embracing industrial policy, steering capital to domestic destinations. For example, the U.S. is providing large subsidies to attract investment in semiconductors, solar, and other futuristic industries. This explains the recent reversal in flows from developing towards richer economies.

The changing geography of industrial investment will be most harmful to emerging markets. Due to inadequate domestic resources (savings, capital markets and currency reserves), these nations rely heavily on foreign investments for sustainable development. A lack of economic heft is forcing these states to pick a geopolitical side or face the risk of losing access to funding.

Partners in a strong marriage can communicate, persevere and grow through their inevitable ups and downs. Cross-border investments must build on foundations of trust, shared values and a commitment to growth—in sickness and in health.

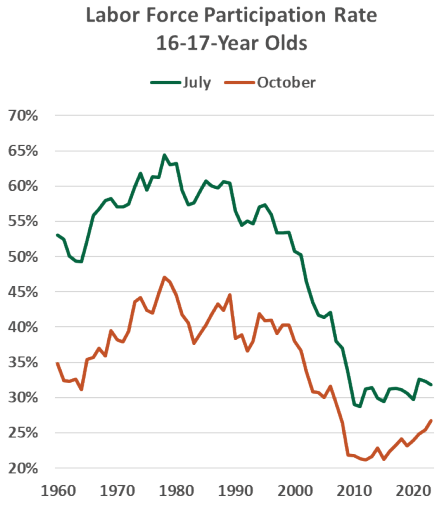
Everyone Remembers Their First

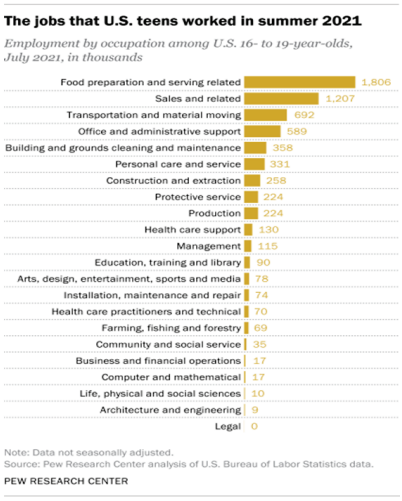
At a recent dinner with clients, the conversation turned to our first summer jobs and early wages. I showed my relative youth by saying I earned the minimum wage, a princely $5.15 per hour when I was 16 years old. The retirees around the table one-upped me with their memories of earning as little as $1.25 when they were teens.

We all agreed that good working habits start young. Even the most basic job will teach the importance of punctuality, having a boss, pleasing customers—life skills that can't be fully conveyed in the classroom. And a bit of extra cash doesn't hurt.

Teenagers have been working less and less during breaks from school. From a peak of over 64%

in 1978, summer labor force participation among 16-17 year olds entered a persistent decline, notably falling by half from the late 1990s to early 2010s. Some of the decline was structural, and welcome: with more jobs requiring a high school diploma, more teens are staying enrolled and graduating, lowering their year-round labor force participation. But recent cohorts face more competition for their summer breaks from sports, volunteering and academic enrichment.





Sources: Bureau of Labor Statistics, Haver Analytics

Teens can help close seasonal labor market gaps.

Today's teens have plenty of opportunities amid an ongoing shortage of labor, especially for entry level roles. Common summer occupations like lifeguarding have faced persistent shortfalls. Immigration flows have not yet caught up with demand for less-skilled workers. The number of job openings in categories like recreation, restaurants and local government (park districts and libraries) are all holding above their pre-pandemic levels.

Recruiting firm Challenger, Gray and Christmas reports a balanced outlook for teen hiring this year. High inflation has added to labor costs, which can make employers more thoughtful about staffing up; after the pandemic hiring rush in 2020, summer jobs gains have cooled. However, as long as consumer demand stays strong, seasonal workers will be needed.

The wages may be paltry; the work may feel menial and demanding. But the value of teens taking those early jobs will be vital for growth: both for young workers individually, and for the economy broadly.

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