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WEEKLY ECONOMIC COMMENTARY

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Global Economic Research
50 South La Salle Street
Chicago, Illinois 60603
northerntrust.com

Carl R. Tannenbaum
Chief Economist
312-557-8820
ct92@ntrs.com

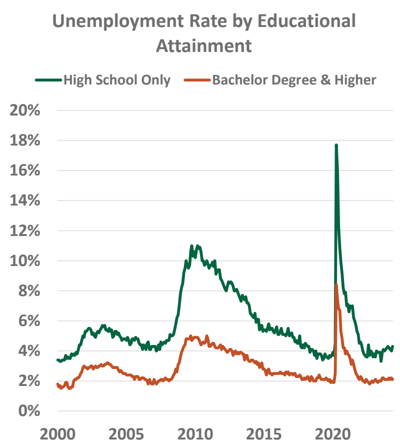
Ryan James Boyle
Chief U.S. Economist
312-444-3843
rjb13@ntrs.com

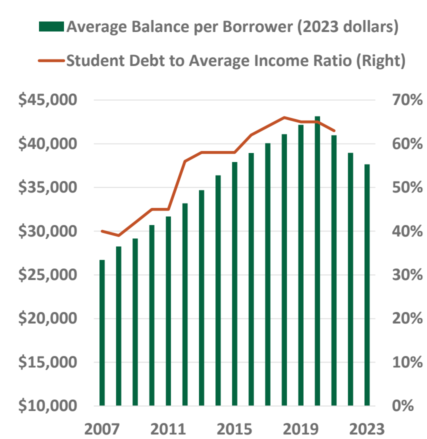
Vaibhav Tandon
Chief International Economist
630-276-2498
vt141@ntrs.com

Language is a living construct. New words are continually added, older words fall out of general usage, and some words change their meanings along the way. On the latter front, some of my younger colleagues use "adult" as a verb. Responsible, necessary but dull activities like paying bills and repairing our homes qualify as *adulting*.

Every June, hundreds of thousands of university graduates make the transition from studying to adulting. Most will now need to focus on finding steady work, living independently and budgeting, with student loan payments occupying a large portion of newly-formed household budgets. As the bills pile up on those young adults, they may be left pondering a difficult question: was my degree worth pursuing?

Not long ago, the question would have sounded absurd. For nearly as along as the data have been tracked, degree holders could expect better employment prospects, higher wages and an all-around higher quality of life for themselves and their future children. Getting a degree was well worth the delayed entry to the working world.





Sources: Bureau of Labor Statistics, Haver Analytics, Education Data Initiative

Today, bachelor's degrees are coming at a high cost. The lowest yearly expenses - at public universities for in-state students - now average $20,000. Elite private institutions are approaching $100,000 per year. In practice, scholarships help many students avoid paying sticker prices, but very few get a full ride. As a result, the average graduate in 2023 started their earning years with debt of $33,500.

Not every enrollment ends with a diploma. Whether the student faced health troubles or simply wasn't ready, an estimated 25% of first-time bachelor's degree seekers leave without finishing a degree. Those students are left with the worst possible outcome: educational debt, no credentials and years of foregone wages and on-the-job experience.

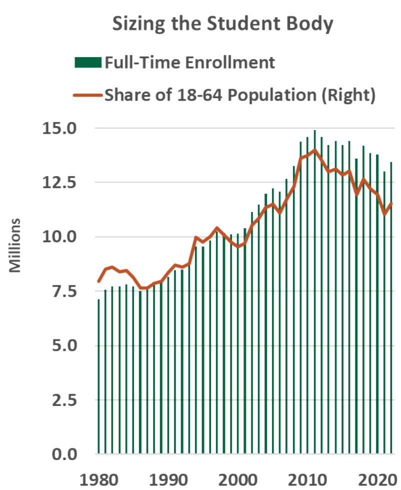
Those students are most likely to end up in default, and may be left living with impaired credit scores.

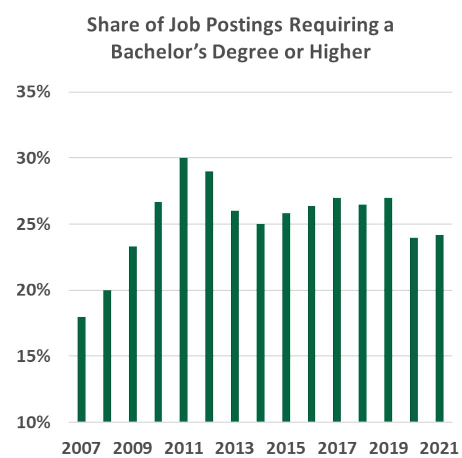
These outcomes have introduced an element of risk to the decision to attend college. More students are deterred by the downside risks of a decision that may feel like a gamble.

Students contemplating college should also consider the risk of their jobs being automated. For a long time, this was a worry limited to workers in factories or other hands-on occupations: machines could do many manual tasks faster and more reliably than a human could. But the gains from automating physical tasks have largely been made. The new generation of artificial intelligence (AI) will compete with the knowledge work that was once considered safe.

AI is in its early stages, but moving quickly. About a fifth of workers may see their jobs disrupted, particularly in specialties like accounting, technical writing and programming. Most workers in these fields believe that AI carries more promise to make them more productive than replace them—but that productivity may be achieved by automating the rote work typically assigned to entry-level roles. Gaining an early-career foothold will become more difficult.

AI is raising the risk of automation to new occupations.





Sources: Census Bureau, Haver Analytics, Burning Glass Institute

The competitive dynamic is already playing out. College enrollment as a share of the adult population in the U.S. peaked around 2010. Smaller universities with more limited curriculum offerings are closing. The decades-long runup of tuition has recently leveled off.

Employers were part of the reason for the push into college, and they are increasingly loosening their requirements for jobs that may not demand degrees. In technical professions like engineering and medicine, undergraduate coursework is highly relevant training for the work ahead. But the degree requirement crept into all roles, meant as a filter to select candidates who could complete assignments and communicate effectively. That is an expensive proxy, and the requirement excludes roughly half the labor force, adding to inequality.

Organized efforts like recruiting candidates who are "skilled through alternative routes," or STARs, are underway. In the looser labor market following the global financial crisis, researchers found 75% of jobs created required a degree, often for roles that were performed by incumbents without degrees. The tight labor market following the pandemic accelerated a more critical look at the actual skills required for a role. Recruiters are now focusing more on applicants' skills than their pedigrees (and may use AI to help sort these additional details.)

Students considering college will have alternatives. Those who are unsure if college is right for them can explore a host of other options. Many in-demand jobs of the future will be hands-on roles like working the production lines of semiconductor fabricators or installing and maintaining a more complex electrical grid; skilled labor, but not requiring college.

A degree is not the only indicator of a candidate's potential.

Building and manufacturing trades are facing a retirement wave of skilled old hands. Inflation has been very high in this cycle in the category of motor vehicle maintenance, due to an ongoing shortage of trained auto mechanics. Well-paying, in-demand trades like plumbing, heating and cooling and electric work are persistently hiring, often filled by immigrants. New joiners in these fields can look forward to paid, on-the-job training, avoiding the burden of student loans.

There are many paths to success; we on our team have put our degrees to great use. Higher education will unlock a beneficial future of upward mobility for most students. But those who choose other paths can also be rewarded. Clear thinking and planning can put more young people on a path toward successful adulting.

At What Cost?

Economists are different from normal people. We think that families use supply and demand curves to decide on whether to have children. We forget the names of our neighbors, but we can identify all of the members of the Federal Reserve Board. We don't think it's funny when someone says that we were created to make weather forecasters look more accurate.

Economists also believe that people make decisions using cold calculus instead of gut instinct. But voters often employ a visceral perspective when considering pocketbook issues. And this could have a significant bearing on the U.S. election outcome.

The American economy and American markets have performed very well over the past two years. Yet surveys reflect a degree of disappointment. Measures of consumer sentiment are still at a significant deficit to their pre-pandemic levels. A Gallup poll covering the President's handling of the economy is at its lowest reading since 2001.

One reason for the disaffection is inflation, which is a leading concern for Americans. This surprises some economists, who point to significant improvement on this front over the past two years. The most recent reading of the Consumer Price Index showed a yearly increase of 3.3%, down from the peak of more than 9% in 2022. Most analysts expect continued moderation in the months ahead.

Further, wages are rising faster than prices. Average hourly earnings are more than 4% higher over the past twelve months, creating gains in real purchasing power for most workers. That should make people happy, but it has not.

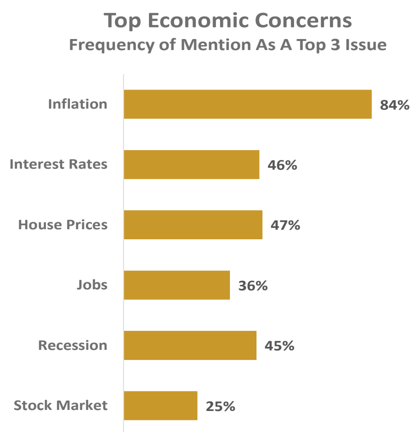
A typical person does not follow the inflation data at close range. Instead, impressions of inflation are formed through the experience of shopping for goods and services. And whether it is strictly rational or not, many think that things have gotten inordinately expensive.

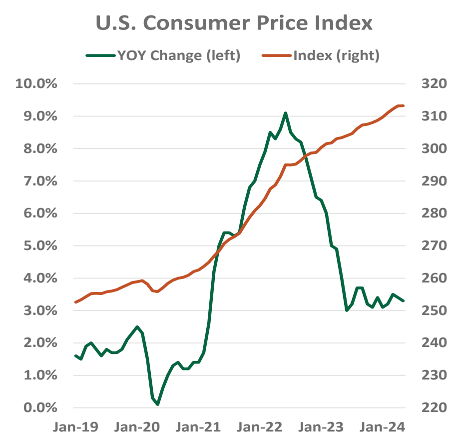
Normal people do not confine themselves to the twelve-month window employed by economists to gauge inflation. In many cases, perceptions are still anchored to pre-pandemic conditions. In aggregate, prices paid by American consumers are more than 20% higher than they were four years ago.

It is also puzzling to laypeople why food and energy prices are set aside when agents like the Federal Reserve assess "core" inflation. These two categories account for a significant portion of monthly spending for many households, and a source of considerable anxiety. A gallon of regular gasoline has averaged $3.41 so far this year, as compared to $2.61 in 2019. Grocery shopping involves regular bouts of disbelief. A dozen eggs costs twice what they did in 2020. Chicken has gone from $1.40 per pound back then to over $2 now. And the list goes on.

Inflation is still viewed as a serious problem by most Americans.

To some, only a decline in prices would signal to them that inflation was under control. While we have seen deflation in spots, prices typically don't retreat. The fact that earnings are rising more quickly than inflation over the past year is of little comfort. Households view this as making up for declines in real income that lasted for more than two years.





Sources: TransUnion, BLS, Bloomberg

Presidents tend to take the blame for economic discontent, even though they often have little influence over outcomes. Post-pandemic inflation was primarily the product of two supply shocks, to the availability of goods imported from the Far East and to the availability of labor. Neither was within the control of the Oval Office.

The Federal Reserve is chartered with keeping inflation under control, but was late to recognize the scale of the problem. The elevated interest rates required to restore order have impaired housing affordability and stretched those carrying credit card debt. The Fed strives to remain apolitical, but its performance since the last election may have a big influence on the next one.

And so while economists cheer the decline in inflation as they see it, households are not feeling cheery. The difference of perspective may make a difference in November.

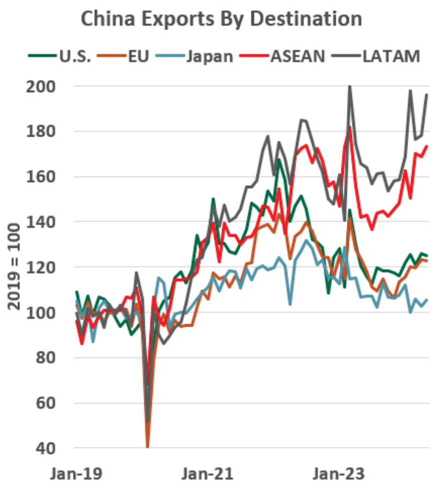
Three's Company

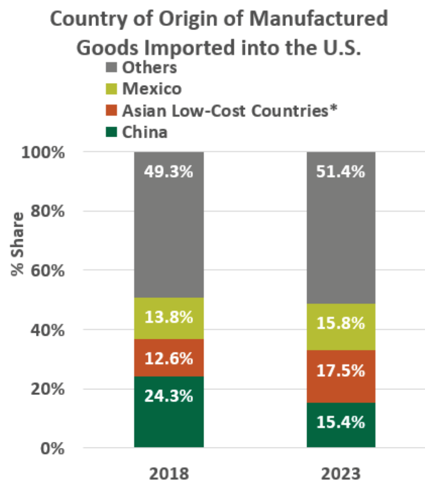
Wedding invitations often include a "plus one," meaning that the guest can bring a guest. There is often intense curiosity over who comes along to the party.

Over the past decade, this term has been appropriated by the architects of trade policy. Fueled by a rise in mistrust between Beijing and the West, COVID-19 and a decline in cost advantages, countries and companies are adopting a *China plus one* business model. Here, too, there is keen interest in who gets invited to the table.

The trend is visible in the decline in China's share of imports to the U.S. and in rising cases of firms setting up new subsidiaries outside China. Large electronics manufacturers and venture capital firms have been shifting investment away from China. About 40% of the more than 500 European firms surveyed have either shifted or are considering moving future investments out of China.

All of this has presented a multi-billion dollar opportunity for other nations. South-east Asian economies, with longstanding ties to both China and America, have emerged as attractive destinations to set up shop. Mexico and India are also among the top contenders due to their links with the West, skilled workforces and business-friendly policies.





*Sources: Haver Analytics, Kearney; *Includes countries like Vietnam, India, Philippines, Indonesia, Malaysia, Cambodia*

China's dominance as manufacturing hub is not at immediate risk, but the competition is getting tougher.

Costs alone may not be the sole driver of business decisions in today's fragmented world. To avoid future disruptions, firms still need to consider the economic and political landscape of the "plus one" nation, such as its currency strength, labor laws, regulations and geopolitical alignment.

To maintain market share, Chinese brands are trying to qualify as "plus ones" by setting up new factories and headquarters outside the mainland to cater to foreign markets. This practice, known as "white labeling," is under investigation among importers seeking to control reliance on China.

The allure of China as a global manufacturing hub is unlikely to fade anytime soon. The country has a strong infrastructure and supply chain network, which allows efficient transportation of goods. Major companies have operations entrenched there, which will be difficult to relocate.

"Plus ones" often represent longstanding relationships, but they can also be more fleeting. Choosing the right partner to dance with is critical.

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@NT_CTannenbaum

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