FedEx chief economist delivers his view of the world

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Gene Huang

Gene Huang is no ivory tower economist. Through his position at FedEx Corporation, Dr. Huang gets timely readings on the health of economies around the world courtesy of a company that delivers more than 9 million shipments daily in more than 220 countries and territories.

The changing levels of these deliveries can reveal signs of growing or falling demand, which is why FedEx's business is widely considered an economic barometer.

In addition to his real-world vantage point, FedEx's chief economist has strong academic credentials. He earned a Ph.D. from the University of Pennsylvania, an M.A. from Yale, and a law degree from Fudan University in Shanghai, China. He is president of the National Association for Business Economics and chairman of the economic advisory committee of Council on Competitiveness.

Vanguard and FedEx have a longstanding connection: Our company provides investments and other services for FedEx's 401(k) employee retirement plan. We interviewed Dr. Huang on August 13, 2012, about the state of the economy, both domestically and internationally. These are excerpts:

What's your outlook for the U.S. economy?

I say it's like the end of a very long boxing match, and both of the boxers are hanging onto each other tightly. You cannot tell who is winning or who is losing, and that has been the situation for a while.

One of these boxers I call "Mr. Positive" and the other "Mr. Negative." Mr. Positive shows a little muscle in housing, in the energy area, and in private balance sheets—so those are probably the top three positive things. Mr. Negative, meanwhile, continues to flash regulatory and fiscal uncertainty, both in the United States and in the Eurozone.

As far as the outlook is concerned, it really depends on how these forces interact. We are looking for modest 2.2% growth in U.S. gross domestic product for this calendar year. Outlook for 2013 will be highly dependent on a few "exogenous" factors, in particular the way the so-called fiscal cliff will be handled. We put a close to 2% number

as a placeholder. [GDP growth has averaged 3.1% annually over the last 50 years.]

What about U.S. employment—do you see improvement?

The labor market is growing. I'm estimating that the economy will add roughly 185,000 jobs per month, on average, for the next 12 months. But we need to do better than that. Jobs aren't growing at a pace that generates an expansionary attitude. And that is mainly because the demand-side picture is unclear and the overall policy environment isn't supportive of investment. For example, there's uncertainty in terms of the corporate tax structure, and in terms of the tax treatment of capital expense and bonus depreciation. It's natural for businesses to have a wait-and-see mentality.

Businesses probably could have taken a more expansionary posture, but because of the uncertainty, there is no way for them to calculate on the cost side. So that is a problem. On the policy side, it seems governments are postponing dealing with issues—kicking the can down the road or, as they say in the U.K., kicking it into the long grass. Until the policy and regulatory side becomes clearer, it's not logical for businesses to make major decisions.

The situation in Europe is very fluid, but do you think the euro common currency will survive?

I've spoken with policymakers and some of the architects of the rescue packages, and my impression is that they understand the cost side will be way too high if the Eurozone faces a breakup. They don't want to go back to the old days, before the common currency.

The reason to have this union is to foster peace among the countries and to promote dialogue and the common interest as well as economic growth. It's a good structure they put in place, but it's incomplete. Now it's a great opportunity for them to work through some issues and refine the structure going forward. So it is not in their interest to dissolve the Eurozone.

That said, I wouldn't be surprised in the next year or so if we have one or two countries leaving the Eurozone. Even if that happens, it's not necessarily a bad thing, and the Eurozone can still avoid a breakup.

The slowdown in China has gotten a lot of attention this year. Is China facing serious economic problems?

With China, what you want to pay attention to are the financial conditions of the government. I would look at that as the number-one thing, given the Chinese government's dominant role in the economy. And the second area I would look at would be the balance sheets of the private sector. Banking deposits are close to 140% of China's gross domestic product. So when I look at that I say, "Whoa!" China has $6.4

trillion worth of deposits, personal deposits. That's huge.

And when I look at the government, the central and local governments combined, I say, "Oh, the fiscal condition is pretty strong." So the country can really afford to even make some mistakes, waste a few resources, so to speak. A slowdown in the industrial sector is taking place in China. It's partly due to a weak external environment and partly by policy design. It's their goal to rebalance the economy, but I wouldn't be worried about a financial-collapse scenario. The private sector, the household sector, is also in good shape. The household savings rate in China is about 40%. In the United States, we are trying to reach 4.5%.

Japan has endured more than 20 years of economic stagnation, despite the efforts of Japan's central bank to revive growth. Is there a risk that the United States could have a similar experience?

When we compare Japan with the United States, yes, there are many similarities. And so this is something we have to be very careful about.

In the past, when we talked about Japan's "liquidity trap" [which occurs when a central bank's injections of cash into the banking system fail to stimulate growth], we used to immediately dismiss the chance of that also happening in the United States. But I think we've come to the realization that we are probably on the verge of a liquidity trap of some kind.

We have to figure out a way to break that mold, and I use three letters to describe the three key areas on which we need to focus. The three letters are "D," "I," and "G"—DIG.

"D" is for demographics. A country's growth potential is more or less determined by growth in the labor force and labor productivity. So if you have a declining labor force, it's a problem. That's what Japan and Europe are facing. In the United States, we are still fortunate that the population is growing, but we have to figure out a way to maintain that kind of growth, especially in skilled labor, and the educated labor force. So I would favor policies designed to encourage more immigration and for us to have more babies. That's fundamental to the country's growth potential.

"I" is for investments. In the United States, we have a great opportunity for improvement in this area. A problem we have is the gap between the ever-increasing consumption share in our gross domestic product and the flat—to somewhat declining—investment share in our GDP. That gap now is satisfied through imports, which creates a trade imbalance and, ultimately, fiscal imbalance.

We have to address this by bringing down the share of consumption in GDP and pushing up the investment share. And the reason that I say this is an opportunity is because our national infrastructure, our roads and bridges, is really old. A lot of it dates from the 1950s, post-World War II, and the population has increased by 100 million since then. So we have to address this. Also, because we are at this beginning of a

revolution in information technology, biotechnology, neurotechnology, and nanotechnology, there are many areas in which we can invest. We have plenty of opportunity to grow this country and to lift the productivity part of the equation.

You have to invest for the future. You don't consume for the future.

And the last part is "G." G is the role of government. Government has to address the debt situation to bring it down to a more sustainable level. And government has to play a role by encouraging innovation and more of a pro-business environment.

So if you put these together, we can "dig" our way to a better future.

Note:

The opinions expressed by Dr. Huang do not necessarily reflect those of Vanguard or its management.