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JOURNAL REPORT
OUTLOOK 2023

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Globalization Isn't Dead. But a Shake-Up Is Building.

Multinational companies still want cheap and efficient markets, but they also want safety. That's why they're rerouting the pathways of global trade and finance.

JON KRAUSE

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BY JON HILSENRATH AND ANTHONY DEBARROS

THE future looked bright to all parties when **Alphabet** Inc.'s Google joined with **Facebook** Inc. and a Hong Kong partner in 2016 to build an 8,000-mile-long undersea fiber-optic-cable line connecting Los Angeles to Hong Kong on an information highway between superpowers.

But the project didn't go as planned. The Trump administration nixed the application for U.S. approval, citing security concerns. Then the tech giants went their own way, routing their pieces of the cable line to the Philippines and Taiwan without the Hong Kong connection.

The shifting path of the Pacific Light Cable Network is a metaphor for the current state of globalization. For decades, multinational companies sought out cheap, efficient supply chains to produce goods for global export, in addition to access to growing young populations in developing countries to spur sales. They operated on the assumption that security and political tensions between countries wouldn't obstruct their operations. That led many of them to China.

These companies are still looking for cheap, efficient and young markets. But now they also want safety, which for many has meant diversification away from direct tension between the world's great economic powers.

In other words, global economic ties haven't ended; they are being rerouted, with widespread

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How U.S. Policies Will Shape Trade

A lot depends on how the U.S. implements last year's measures

BY YUKA HAYASHI

IN just over a year, the U.S. has passed three huge budget measures aimed at transforming its domestic economy—by rebuilding infrastructure, accelerating a clean-energy transition, and boosting manufacturing in semiconductors and the automotive industry.

Each of these initiatives is focused on strengthening the U.S. economy and on boosting U.S. competitiveness in the world. But there is another crucial consideration as well: How these three policies are implemented in the months ahead could reshape global trade relations for years to come.

If U.S. policy makers use this opportunity to promote domestic industries at the expense of foreign competitors, other governments are likely to respond with their own protectionist policies, leading to a costly breakup of global trade, government officials and trade specialists say.

But, these same experts say, if instead the U.S. is more welcoming to products from friendly nations, and works with them to achieve what some call "friend shoring"—shifting production of critical materials to friendly nations, away from adversaries including China and Russia—the countries could continue to enjoy the benefits of trade while strengthening their supply chains, these people say.

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PRICE CHECK

Why inflation may be a more lasting problem than many investors are now assuming. **R2**

Scan this code to hear how last year's confusing economic indicators will affect what's ahead in 2023.

Long Fight

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NEW TRADE ORDER

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STREETWISE | JAMES MACKINTOSH

Four Reasons Why Inflation May Be a Long-Term Problem

Investors don't appear to be worried about rising prices. Perhaps they should be.

IN 1974, historian and sometime presidential speechwriter Arthur M. Schlesinger Jr. summed up the problem with contemporary forecasters in a single, very long sentence in The Wall Street Journal: "To this moment most economists, businessmen and government officials obstinately regard inflation not as the structural vulnerability of contemporary capitalism but rather as the accidental result of unlucky coincidences requiring only patience, time (and unemployment) for its alleviation."

Were Prof. Schlesinger alive today he could not have put it better. The basic assumption of mainstream financial thinking is that inflation is temporary and will be cured by a swift course of higher rates prescribed by the Federal Reserve. Yet, there are plenty of grounds for thinking that, just as in 1974, the professor is right, and the inflationary pressures will last.

This is not to say that there are no unlucky coincidences. In 1974, inflation was boosted by rates that were too low for years and soaring energy prices due to the Arab oil embargo. Over the past couple of years, inflation was boosted by rates that were too low, a postpandemic supply-chain crunch and soaring energy prices due to Russia's invasion of Ukraine. As in 1974, these temporary factors will pass, and the latest drop in inflation suggests many of them already have. But as in the years after 1974, deep-rooted structural vulnerabilities may mean that inflation remains a problem for years to come.

There are four big risks: geopolitics, domestic politics, demographics and the Fed. The first three help determine where rates need to be to combat inflationary pressures, while the Fed's willingness to raise rates helps determine whether inflation rises or falls.

The great divide

The new geopolitics is splitting the world into two blocs, partially reversing the globalization of the past three decades. That means more investment is needed to recreate production lines and supply chains that bypass China, while efficiency is likely to fall, as security issues rather than cost dictate location. Subsidies for chip factories in the U.S. and Europe are the obvious expense to society, but barring some new detente, similar subsidies are likely to spread to other high-tech sectors. Doubling up production and supply chains directly reduces productivity, meaning more inflation for the same amount of economic growth.

Geopolitics is also likely to bring more spending on weapons. War on the borders of Europe has led to bigger military budgets in the region, even without the cost of weapons being sent to Ukraine. Since the military doesn't boost productivity, increased spending adds to upward pressure on inflation.

On the domestic front, efforts to reduce global warming will continue to increase spending in the push to reduce fossil fuels. Some of that may help efficiency, if energy production costs fall far enough below current levels, but much of it won't. Added security again will come at the cost of efficiency.

Tanks in Poland, a wind farm in the U.S. Higher spending on weapons and energy alternatives will add to pressure on inflation.

Domestic politics in the U.S. and Europe appear to have switched from free-market capitalism to more government intervention and industrial policy. In the past that has often led governments to misdirect finance toward supporters or to trendy projects. Governments find it embarrassing to back away from failures. Badly directed investment reduces productivity, increasing inflation pressure.

Demographic shift

Finally, demographics is working to push up inflation. After decades of adding tens of millions of well-educated, low-cost workers to the global economy every year, China has seen its working-age population begin to shrink. The additional global production that China delivered as it opened up helped control inflation during the years of "great moderation," but won't be repeated. Along with renewed interest in trade unions, it could lead to a shift of bargaining power back to workers, again pressuring inflation.

None of this matters if the Fed is willing to do what it takes to control inflation, points out Olivier Blanchard, a former chief economist of the International Monetary Fund now at the Peterson Institute for International Economics. "Central banks are totally committed to getting inflation under control," he says. "The issue is whether they go back to 2% or do they aim for something slightly higher."

I'm less convinced that central banks will be willing to lift interest rates enough to get inflation back to superlow levels if the trends outlined above continue. Mr. Blanchard says a rough guideline is to assume that every additional 1% of GDP that goes into investment means the real, after-inflation interest rate needs to be 1 percentage point higher. Treat military spending as akin to investment—albeit with no return—and it could easily add 1% of GDP on its own, or more than double that to return to 1980s Cold War levels. A serious effort to stick to the Paris goals on climate change could add another 1% to 2% of GDP, and that's before spending to remove China from supply chains.

Investors don't think any of this will be a problem. Bond markets are priced on the premise that inflation will rapidly fall back to the Fed's 2% target and stay there, without the Fed needing to do anything really dramatic.

Sure, real Treasury yields are much higher than their pandemic lows, when investors were willing to lock in a return below inflation for 10 years using Treasury inflation-protected securities, or TIPS. But the 10-year TIPS yield at 1.3% or so remains well below the 2.1% it averaged from 2004 to 2007, a time when China trade was helping cut inflation and German military spending reached a postwar low.

Not everything that was holding down inflation is now pushing it up. Technology helped keep a lid on inflation by making comparison-shopping easier and revolutionizing supply-chain management. Tech such as artificial intelligence, gene therapy and low-cost rocketry might help ease inflationary pressures, too.

But many of the factors that once helped central banks have gone into reverse, and investors are ignoring them. Markets are not prepared for the higher rates required if inflationary pressures prove persistent, as I expect. Worse, central bankers might not be prepared to take flak from a society that has become reliant on easy money, and may quietly accept price rises higher than their targets. If either happens, bond yields will be higher and, most likely, stocks lower than they would be otherwise.

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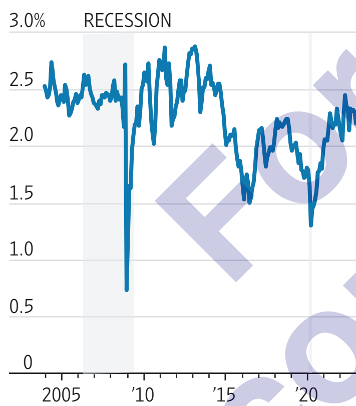
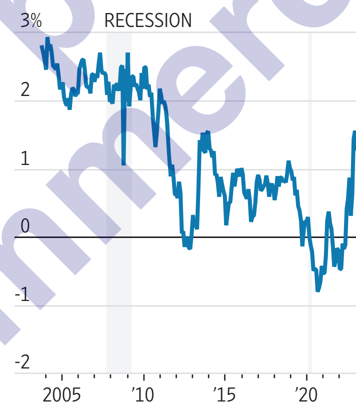
Inflation Magic

Bond markets expect long-run inflation to be lower than before the 2008-09 financial crisis, with interest rates lower, too

Five-year inflation breakeven starting in five years



Five-year real yield starting in five years



Note: Monthly data derived from Treasury inflation-protected securities
Sources: Federal Reserve Bank of St. Louis (inflation); Refinitiv (real yield)

FROM TOP: MATEUSZ SLODKOWSKI/AFP/GETTY IMAGES; M. SCOTT BRAUER/BLOOMBERG NEWS

A Q&A With Klaus Schwab

He founded the World Economic Forum in 1971. Here's how he sees the state of the world now.

THE past year brought war in Europe, surging inflation and an energy crisis, all while the world is still fighting the Covid-19 pandemic and related disruptions. Company executives are evaluating global supply chains and considering what they could make closer to home.

The Wall Street Journal's editor in chief, Matt Murray, and Journal reporter Thomas Gryta sat down with World Economic Forum founder Klaus Schwab in November as he prepared for his 53rd annual confab in Davos, Switzerland this month. Mr. Schwab, age 84, launched the WEF as a young academic in 1971, but it is now an independent international organization under the Swiss government, similar to the Red Cross. Edited excerpts of the conversation follow.

• WSJ: When you think about the state of the world and the themes of this year, what stands out to you?

• MR. SCHWAB: When we look at the crisis we are in, I see it less as a crisis in the usual sense. I see it as a whole transformation of our global system.

If we take the economic side, I would say we will go through a very difficult three-, four-, five-year transformation period. And the forces behind this? Of course, the war in Ukraine. And even if we solve the war, it will be reconstruction. You have the energy transformation or transition. You have the reshaping of the global supply chains. You have the post-Covid effects, which some people say are lower productivity and of course the need to invest more into resilience.

If you take all those economic forces, they bite into the purchasing power of people because, at the moment, there are costs.

If you are a company, you write it off in your balance sheet, and the shareholders are those who suffer.

We have to address this transformation, not with a crisis mentality, to have simple solutions for very complex problems, but we have to look long term.

• WSJ: Do you see the world becoming more about more regionalized blocs that cooperate in some areas and compete in other areas?

A period of transformation is ahead, Mr. Schwab says.

• MR. SCHWAB: Yeah, if I would look at the political dimension of this transformation, I would argue we are going into a multipower world.

Of course, you have two superpowers, but then you have the emerging superpower like India. You have the blocs like Europe, which, in my opinion, has become stronger despite Brexit in the last three years. We should not underestimate other Asian countries. Then you have the rogue states like North Korea and Iran. Then you have what I would call the fast fish, small countries moving fast and being some kind of role models for other countries, like Singapore, and to a certain extent, Israel.

Then you have the corporate powers, which play a substantial role, and I would even add the social communities. It will be a very complex, messy world.

• WSJ: Do you think, when you talk about models beyond country models, is it time for new multinational institutions and new models?

• MR. SCHWAB: Our existing institutions do not suffice in the world of today. One missing element is, for example, to integrate the other important stakeholders like business, media and so on into the discussions. In Davos, you will see a presentation of what we call the global collaboration village. We have created a supporting community of over 70 companies and international organizations like the International Monetary Fund or World Trade Organization to create a kind of Davos in the metaverse, in the virtual world, to have a possibility to continue the dialogue but to widen the dialogue to integrate more stakeholders.

I think what is needed is a trusted informal platform where you can speak much more in open ways and really address the issues, not in a political way, but with a will to find a solution.

• WSJ: You said you were not surprised that there's been a backlash on some of the globalization trends. But do you think that we're in a period where we're fundamentally resetting some of the precepts? Or do you think it's a passing reaction?

• MR. SCHWAB: I call it reglobalization. The world is becoming more interdependent, but on the other hand, we will have relations much more on the basis of trust, because we are not able to create the necessary norms, the necessary rules, which we can share. The future of the world could be a kind of patchwork of coalitions which are trust-based.

BEAT SCHWEIZER FOR THE WALL STREET JOURNAL

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OR INVEST IN TECH?

DO THE RIGHT THING
OR DO THE PROFITABLE THING?

SATISFY SHAREHOLDERS
OR SATISFY CUSTOMERS?

ELEVATE EXPERIENCES
OR LOWER EXPENSES?

WORK WITH LESS
OR DO MORE?

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Is the West Ready for a Long War?

Time could be on Russia's side in Ukraine if the U.S. and its allies don't adjust to a prolonged conflict

BY YAROSLAV TROFIMOV

THE war in Ukraine, it's clear by now, won't end soon. The bet in Moscow—and the fear in Kyiv—is that the West will lose stamina before Russia suffers a decisive defeat.

So far, Russia's expectations of discord among Ukraine's backers haven't materialized. Europe has severed its dependence on Russian energy with limited pain. As all major Western economies grew in 2022 despite the disruptions, the consensus behind supplying weapons to Kyiv has only solidified.

Yet, with Russia announcing a mobilization of hundreds of thousands of soldiers in September and switching its economy to a war footing, time could be on Moscow's side. So far, neither the U.S. nor Europe has made the adjustments, especially in military production, that are necessary for sustaining Ukraine in a war that could potentially drag on for several years. Neither are they immune to pain from further energy shocks.

"The idea that a major classic conventional war in Europe could last as long as one of the two world wars is not something we are yet ready for," says Bruno Tertrais, deputy director of the Foundation for Strategic Research, a Paris think tank. "Even though the resilience of European societies has been remarkable, it cannot be taken for granted."

A new Congress

The same goes for the U.S. While the lame-duck Congress in December authorized $44.9 billion in funding to support the war in Ukraine, probably enough for the next nine months, the new Republican control of the House means that further military and civilian aid packages for Kyiv may be more complicated to fund.

If time works to Moscow's advantage, it's in the West's interest to dramatically increase support for Ukraine in coming months, abandoning the excessive caution that characterized weapons deliveries until now, says retired Air Marshal Edward Stringer, former head of operations at the British Defense Staff.

"By continuing to drip-feed just enough for Ukraine not to lose, what the West is doing is just prolonging the war," Air Marshal Stringer says.

Ukraine's own once-significant defense industry has been decimated by Russian airstrikes, and the country now is almost wholly reliant on Western-provided weapons and ammunition to survive. While Russia's economy, roughly the size of Spain's, is a minnow compared with the combined might of the U.S. and its NATO allies, Western defense procurement and manufacturing—unlike Russia's—is largely continuing to follow peacetime procedures and schedules.

"The West, in general, naturally overshadows Russia in economic potential and defense-industrial capacity, and that should make you believe that, in a protracted war, Ukraine with Western support stands a much better chance of winning the conflict," says Michael Kofman, director of Russia studies at the Center for Naval Analyses, a think tank that advises the U.S. military. "But that is not a predetermined outcome. Potential is just that. It takes a great deal of will, and wars are fundamentally a contest of wills."

Ukrainian soldiers near Bakhmut, site of a Russian counteroffensive.

LIBKOS/ASSOCIATED PRESS

Manpower math

Before last fall's mobilization, Russia suffered from manpower shortages in Ukraine while relying on an overwhelming advantage in artillery firepower. Now that Russia has mobilized 300,000 reservists, it has solved its manpower problem just as it's starting to run low on ammunition and materiel.

Long term, the arithmetic of manpower works to Moscow's advantage as Russia has 3.5 times Ukraine's population. Even if Russia loses two soldiers for every one Ukrainian service member killed, it still improves its relative strength. So far, Western officials say, Russia's battlefield fatalities—numbering in several tens of thousands—are comparable to Ukraine's.

The calculus on ammunition and weaponry is more complicated. Ukraine uses up Western-supplied 155 mm artillery shells at roughly twice the rate that they are being manufactured by the U.S. and allies, military analysts say. At this rate of fire, Kyiv could draw down U.S. and European reserves to critical levels at some point this summer or fall.

By then, Russia may be able to expand its own ammunition production to keep pace with the tempo of the fighting. The U.S. and allies are also investing in new ammunition production lines, but these are unlikely to make a major difference until next year, creating a potentially dangerous gap between Ukraine's and Russia's firepower in the second half of 2023.

An existential fight

Russia's mobilization has already allowed Mr. Putin to stabilize the front line, and to launch a counteroffensive around the city of Bakhmut in the eastern Donetsk region. Possibilities of a negotiated settlement are remote in the foreseeable future.

"Any notion of the peace process is out because Putin is doing everything to make clear that this is existential for him," says Ivo Daalder, a former U.S. ambassador to NATO who heads the Chicago Council on Global Affairs. With no end to the conflict in sight, he says, the U.S. and allies should start preparing to integrate the government-controlled majority of Ukraine into Western institutions, without waiting for the war's conclusion.

Ukraine says its war aim is to oust Russia from all territories conquered in the past year and from the areas it lost to Russia in 2014, including Crimea. Ukraine regaining even part of these areas would endanger Mr. Putin's hold on power at home.

Russia seeks, at a minimum, to conquer the Ukrainian-held parts of Ukraine's Donetsk, Luhansk, Kherson and Zaporizhzhia regions that Mr. Putin declared to be part of Russia in October. Almost the entire front line now runs across what Russia considers to be its own sovereign soil.

Ukrainian officials warn that Moscow's initial war goal, the occupation of Kyiv and the entirety of the country, hasn't changed—and that any pause in the conflict would be used by Mr. Putin to regroup and strike again.

"They are preparing for new battles, for new offensive operations, not for talks. Nothing speaks in favor of Russia being ready to talk," says Ukraine Foreign Minister Dmytro Kuleba. "I know Russia, I see what is happening in Russia. And I think it's either them or us. There is nothing in between now anymore."

Mr. Trofimov is the chief foreign-affairs correspondent of The Wall Street Journal. Email yaroslav.trofimov@wsj.com.

Travelers in Hong Kong as the border with mainland China reopened.

LAM YIK/BLOOMBERG NEWS

China Faces a Rocky Emergence From the Zero-Covid Era

Xi Jinping confronts instability at home and abroad

BY CHUN HAN WONG

CHINESE leader Xi Jinping went from cementing his supremacy last fall to battling a public-health and economic crisis into the new year—fallout from an abrupt pivot from "zero Covid" that could cast a shadow over China for months.

Mr. Xi secured a norm-breaking third term as Communist Party chief in October, and stacked the leadership with allies who sang their leader's praises and trumpeted his vision of a thriving China. That rosiness dissolved amid intensifying economic pain and a wave of public protests against Mr. Xi's zero-tolerance Covid strategy of lockdowns and border controls, followed by a haphazard dismantling of pandemic protocols that threatens to further batter the world's second-largest economy.

Some analysts describe China's tumultuous exit from zero-Covid policies as largely self-inflicted pain, exacerbated by Mr. Xi's domineering style. The repercussions could be profound for Mr. Xi, who had touted his pandemic strategy as an example of the Communist Party's superior governance.

"This is likely to be a year of turbulence for Xi Jinping," says Alfred Wu, an associate professor at the Lee Kuan Yew School of Public Policy in Singapore.

The party's energies are set to be consumed managing the economic and social impact from the end of zero Covid, as well as restoring public trust, Mr. Wu says, adding, "Xi claims all the credit but deserves all the blame, too."

Seeking 'reasonable' growth

Chinese leaders promised to deliver "reasonable" economic growth in 2023, calling on officials to stimulate domestic demand while signaling plans to further ease regulations that have triggered a downward spiral in the property market and hampered private business investments.

Mr. Xi also brooked no criticism of his top-down methods. At a Politburo meeting in December, Mr. Xi insisted on "absolute loyalty" to his leadership "under any circumstance," while appearing to blame local officials for faulty implementation of his policies.

Many economists expect a fraught year ahead for China, citing the risk of surging Covid-19 infections disrupting supply chains and overwhelming the healthcare system. Though some analysts forecast a rebound in commerce and consumption after fresh outbreaks subside, possibly in the spring, it remains to be seen how firm this recovery will be.

Tentative consumers

Chinese consumers appeared tentative as 2022 drew to a close. Domestic trips edged up 0.4% over the New Year holiday weekend compared with a year earlier, while tourist spending ticked up 4%. Movie box-office receipts fell more than 45% year-over-year.

Beijing also faces an uphill battle in rebuilding confidence among businesses, which increasingly regard Mr. Xi's government as capricious in setting policy, says Jörg Wuttke, president of the European Union Chamber of Commerce in China.

In a 2022 survey of its members, the EU Chamber said 60% of respondents reported increased difficulties in doing business in China, compared with 47% in the previous year, in part due to the opaque regulatory environment and the increased politicization of business. "We associate China with a very well-planned, well-organized government, and all of a sudden we see it capitulate in the face of Omicron," Mr. Wuttke says. "That takes away a lot of trust in the government's abilities."

The onus therefore falls upon the Xi administration to restore public confidence, economists and business groups say. "Chinese citizens know who is in charge," says Andrew Collier, managing director of Orient Capital Research in Hong Kong. "The huge death toll, coupled with the collapsing property market, are going to test the people's trust in Beijing in 2023."

60%
of European companies in China reported increased difficulties doing business there in 2022, up from 47% the prior year

Nearly 250 million
people in China were infected with the coronavirus between Dec. 1 and Dec. 20, according to notes of a National Health Commission meeting seen by The Wall Street Journal

45%
Decline in movie box-office receipts in China over the New Year's holiday weekend from a year earlier

Sources: European Union Chamber of Commerce in China (60%); WSJ; Lighthouse (45%)

International tensions

On the diplomatic front, Beijing's transition to a postpandemic future has raised hopes that a revival of cross-border interactions could help mitigate geopolitical tensions with the West.

China's ties with Western governments remain fraught over Beijing's support for Moscow throughout the Russian invasion of Ukraine. Tensions with the U.S. still simmer even as Mr. Xi and President Biden, who met in November, pledged to restore dialogue and a measure of stability in a fractious relationship.

Beijing, which claims Taiwan as its territory, continues to regard with deep suspicion U.S. efforts to strengthen cooperation with the island. Since then-House Speaker Nancy Pelosi's August visit to Taipei, which China condemned, the People's Liberation Army has conducted an array of combat drills that showcased capabilities to cut off Taiwan. Nonetheless, the Biden administration has pledged to continue providing arms and training to help Taipei defend itself.

Notwithstanding recent setbacks, Mr. Xi seems set to double down on his priorities, says Mr. Wu, the Singapore-based academic. "In difficult times like these, he often emphasizes the need for greater 'fighting spirit,' and insists that they must overcome any challenges."

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CAPITAL ACCOUNT | GREG IP

Who Is Going to Police the New World Trading System?

As the WTO is increasingly sidelined, the future is going to look more like the past

THE globalization boom that began in the 1990s didn't happen by itself: It was lubricated by the biggest economies' willingness to write, enforce and obey shared rules of engagement.

That consensus is now crumbling. The World Trade Organization, the embodiment of this rules-based order, has increasingly been sidelined as countries turn to export controls, subsidies and tariffs to promote domestic industries or kneecap adversaries.

Many blame this on the U.S., as first President Trump and now President Biden rejected WTO authority and enacted tariffs and subsidies that riled trading partners.

Poor fit

In reality, the WTO's credibility began to erode much earlier with the rise of China, whose authoritarian, statist economy has proved incompatible with the trading system the market-based democracies built after World War II.

Mr. Biden has governed as a champion of the international order, yet on trade, he has stuck with many of the policies enacted by the avowedly nationalistic Mr. Trump. He has maintained Mr. Trump's tariffs on China and blocked appointments to the WTO appellate body, which has the final say on enforcement decisions, leaving it unable to function.

Last month, in two separate decisions, WTO panels ruled that the Trump administration had violated its WTO obligations by imposing tariffs on imported steel and aluminum, and requiring that products made in Hong Kong be labeled as made in China. The WTO allows a member to impose trade barriers in the interests of its national security, but the U.S. had not met the criteria, the panels said.

A spokesman for U.S. Trade Representative Katherine Tai criticized the decision. The WTO, he said, had no right to even rule on the U.S. actions. The U.S., he noted, has for more than 70 years insisted that it, not the WTO, gets to decide what qualifies as national security.

Systemic tensions

This clash exemplifies the tensions chipping away at the world trading system. Under the WTO and its predecessor, the General Agreement on Tariffs and Trade, members tacitly agreed not to invoke national security, says William Reinsch, a trade expert at the Center for Strategic and International Studies. That tacit agreement no longer exists. If others follow U.S. precedent, "the whole system is useless: It invites everyone to make a national security claim every time."

The European Union has also threatened to take the U.S. to the WTO because the law dubbed the Inflation Reduction Act only provides subsidies to electric vehicles assembled in North America. Beijing has filed a case over U.S. restrictions on exports of semiconductor technology to China.

Yet complaints about U.S. behavior is at best a partial diagnosis of what ails the world trading system. A more complete picture needs to address why the Americans have become so obstreperous.

The U.S. had originally pushed for the WTO's binding dispute mechanism out of frustration that under its predecessor, GATT, enforcement decisions could be easily blocked by any one country.

The unintended consequence is that countries unhappy with U.S. trade laws, rather than negotiate, sue the U.S. at the WTO, and often win because WTO judges take an expansive view of their own authority to interpret and, critics say, make trade law.

As frustrating was the WTO's inability to discipline China's protectionist and discriminatory practices.

In market democracies, for example, the state deals with companies at arm's length, and subsidies are transparent and rules-based. In China, there is no bright line between the state and the private sector. Subsidies are pervasive and opaque and thus difficult to police.

For example, for years only electric vehicles equipped with batteries made by Chinese companies qualified for Chinese government subsidies. But as Brad Setser of the Council on Foreign Relations notes, because this discriminatory behavior wasn't codified, a violation in trade laws was hard to prove—in contrast to the U.S., where subsidies are written into laws and regulations.

A WTO complaint typically requires evidence a company was harmed. But Western companies that complain about their treatment in China can expect the government to retaliate—for example through an antitrust or cybersecurity investigation—and thus they stay silent. China routinely punishes countries that cross it diplomatically by blocking imports or tourism, without making a formal connection. This makes it hard to bring a WTO complaint.

The net result is that today the WTO is unable to discipline either its largest or second largest member, leaving a deglobalizing world without an effective cop on the trade beat.

Where it leads

This doesn't portend a return to the 1930s, when countries dramatically raised tariffs and retreated into autarky. The WTO still exists, and most members still abide by their commitments.

Some have used alternative channels to adjudicate disputes while the appellate body remains defunct.

U.S. officials say their imposition of trade barriers on national-security grounds won't precipitate a flood of frivolous copycat actions. Any country making such a claim accepts the right of affected trading partners to retaliate—and would thus think twice. "There's a self-regulating nature to invoking national security," one official says, noting that the U.S. faced retaliation for its steel and aluminum tariffs long before the WTO ruled.

Rather than a single set of rules imposed on fundamentally incompatible systems, such as China's and the U.S.'s, the world will migrate toward a series of regional pacts. This lets countries pick partners and sectors where their values and interests happen to align, such as Singapore's digital trade agreement with Australia. The Biden administration's Indo-Pacific Economic Framework represents a la carte economic cooperation: Participating countries pick from a menu of fields in which to participate—tax, infrastructure, supply-chain resilience and trade.

Dispute settlement mechanisms will still matter. The U.S. and Canada have each won disputes before panels formed under the U.S. Mexico Canada Agreement, over dairy and solar products, respectively. On Wednesday, a USMCA panel sided with Mexico and Canada in finding the U.S. had applied too strict a definition of North American content to automobiles. A spokesman for Ms. Tai said, "We will engage Mexico and Canada on a possible resolution to the dispute."

But the future will resemble the pre-WTO past in that many disputes will be resolved through negotiation rather than litigation. U.S. officials point to the resolution with the EU of a long-running fight over each other's subsidies for commercial airliners, which includes a joint approach to dealing with China. Ms. Tai has suggested Europe respond to U.S. electric-vehicle subsidies by introducing its own. The implication: Rather than sue each other in pursuit of a world without subsidies, the U.S. and Europe should accept that China has made such a world unattainable.

One thing this won't be is a level playing field. Just as hockey without referees favors the team with the largest players, trade without binding dispute settlement favors those countries best able to retaliate, or withstand retaliation—i.e., the U.S., China and the EU. Smaller countries must accept whatever these bigger countries offer.

"This is the U.S. going back to 'Might makes right,'" says Jennifer Hillman, a trade expert at Georgetown University who has also served as a panelist in trade disputes, including at the WTO. "If you're a large country with a significant ability to retaliate, it's self-limiting. If you're a small country, I'm not sure how much difference it makes to have the right to retaliate."

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BRIAN STAUFFER

Trade Policies

Trade-harming vs. trade-liberalizing actions taken by countries by year

5,000 / 4,000 / 3,000 / 2,000 / 1,000 / 0 — Harming — Liberalizing — 2010 / '15 / '20

Note: Trade-harming policies are those designed to hurt competitors, usually by restricting imports or promoting exports. Reporting lags understate the totals for recent years.
Source: Global Trade Alert

How U.S. Will Reshape Trade

Continued from page R1

"Friend-shoring is a rebuttal to those who argue that economic security can be achieved only through protectionism," U.S. Treasury Secretary Janet Yellen wrote in December in an essay on Project Syndicate, a website that carries opinion pieces.

Three bills

America's most significant industrial-policy push in decades takes the form of three bills Congress passed since November 2021. The roughly $280 billion Chips and Science Act promotes domestic semiconductor research and production. The measure known as the Inflation Reduction Act directs about $369 billion to clean energy and energy-security programs. And much of the $1 trillion infrastructure bill will be spent on boosting the U.S.'s economic competitiveness. Calling them down payments for the future, Biden administration officials have said the policies will fuel growth, rebuild fragile supply chains, address climate change, shore up domestic manufacturing and provide good-paying jobs for U.S. workers.

"Add these developments to the ongoing trade friction between the U.S. and China, and global trade is likely to look very different in 2023 and beyond than it did just a few years ago," says Ted Murphy, a trade lawyer for the Sidley Austin firm.

Mr. Murphy expects each initiative to contain various forms of preferential treatment for domestic U.S. manufacturers of critical products, likely causing other governments to pursue their own domestic-production incentives and subsidy programs. This will make it harder for some companies to sell products produced elsewhere, he says.

"Where you produce is increasingly going to matter more, " Mr. Murphy says.

Washington's renewed focus on domestic industry comes after the pandemic, Russia's invasion of Ukraine and rising tensions with China all highlighted the fragility of global supply chains and the danger of relying on a small number of suppliers in a few countries for critical products such as medical supplies, natural gas and advanced semiconductors.

The shift in policy is also a clear departure from the U.S. longstanding promotion of global trade to lower production costs and the price of goods.

U.S. Trade Representative Katherine Tai said in an October speech that the traditional approach to trade, marked by market liberalization and tariff elimination, had imposed "significant costs" on America's economy and society. Among them, she said, were concentration of wealth, fragile supply chains, deindustrialization, offshoring and the decline of manufacturing communities. "The need for correction is clear, and industrial policy is part of that rebalancing act," she said.

Quick pushback

Nevertheless, criticism of the shift in U.S. policy has quickly emerged. The European Union, Japan and South Korea all have demanded the U.S. revise its electric-vehicle tax-incentive program, saying the local-assembly and local-content requirements to qualify for tax credits of up to $7,500 per vehicle discriminate against their companies and might violate World Trade Organization rules.

New U.S. tax incentives for EVs have drawn criticism from other countries.

JEFF KOWALSKY/AGENCE FRANCE-PRESSE/GETTY IMAGES

European Commission President Ursula von der Leyen said in a Dec. 4 speech that the U.S.'s EV program could "redirect" investment flows of manufacturers to the U.S. from Europe at a time when the European economy is reeling from an energy crisis caused by the war in Ukraine.

In a joint paper issued Dec. 19, Bruno Le Maire, France's finance and economy minister, and German Economy Minister Robert Habeck, proposed urgently experimenting with ideas for subsidies and tax credits for key industrial sectors. "We will mobilize all relevant national and European tools and instruments," they wrote.

~$280 billion
The size of the Chips act promoting domestic semiconductor research and production

~$369 billion
Funding for clean energy and energy-security programs in the Inflation Reduction Act

$1 trillion
Size of the infrastructure bill, much of it to be spent on increasing U.S. economic competitiveness

1%
The World Trade Organization's latest projection of global trade growth in 2023, down from a prior projection of 3.4%

The Chips act as well must compete with EU, Japanese and South Korean plans to promote domestic semiconductor industries. Economists and industry executives warn that expanded production fueled by uncoordinated subsidy programs would result in global overcapacity.

Moves by rich nations to retrench from global trade have alarmed international organizations tasked to oversee global economic growth. Officials at such agencies have warned that such steps would only increase inflationary pressure and declines in economic growth and living standards over time. People in developing nations, in particular, are seen as getting hurt.

"If we want to deal with climate change in a collaborative fashion, if we want to deal with preparing for the next pandemic and so on, let us dial down the talk on decoupling and fragmentation," Ngozi Okonjo-Iweala, director-general of the World Trade Organization, said on a December panel at the International Monetary Fund. "It will be very costly to the global economy," she said.

The WTO recently lowered to 1% its projection for growth in total exports and imports for 2023, down from 3.4%.

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Globalization Isn't Dead, but It Is Changing

Continued from page R1

implications. The efficiencies lost mean higher costs for households and businesses, and profit-margin pressure for companies. In boardrooms, it means more attention needs to be paid to risk and a widening landscape of potential crises. For politicians, it will accentuate the struggle to balance economic growth and low inflation against the demand to defend national interest.

However, there are also opportunities. The U.S. energy sector is gaining market share as Europe shifts away from dependence on Russia. At the same time, Vietnam, Philippines, Mexico and others are gaining export business as multinationals diversify their supply networks.

"What we are witnessing is not a collapse of globalization. It is more a reshaping of it," says Dani Rodrik, a Harvard University professor, whose 1997 book, "Has Globalization Gone Too Far?", was among the first to warn of the risk of popular backlash against globalization.

By the numbers

World trade as a share of overall economic activity peaked at 61% in 2008, at the apex of China's power, when a global financial crisis that started in the U.S. caused a worldwide recession. Trade has since receded to 57% of economic activity, according to World Bank data, still far greater than estimates of 31% on average during the 1970s, 36% during the 1980s or 40% in the 1990s.

Mr. Rodrik, for one, doesn't expect to see global trade slump to anywhere near the approximately 10% of economic output that took place in the 1930s. Multinational companies have invested too much in global supply chains to allow them simply to disappear. The costs, in terms of inflation, lost productivity and lost profits, would be too great. Households, valuing access to inexpensive goods, have something at stake in the preservation of globalization, too. Moreover, global bonds are enabled by the inexorable advance of technology.

Instead, it's in the pathways of global trade where you already can see the biggest changes, hastened by the Trump administration's 2018 tariffs against Chinese imports, and then amplified by the Biden administration's efforts to block Chinese imports of advanced U.S. technology, China's self-imposed Covid-related business shutdowns, and Russia's invasion of Ukraine.

The result is that China's share of U.S. imports dropped from a peak of 22% in 2017 to less than 17% last year. Other Asian economies and Mexico are gaining share—most notably Vietnam, whose exports to the U.S. rose from less than $10 billion before 2007 to more than $120 billion in 2022. The Philippines, Taiwan, Thailand, India and Malaysia have also enjoyed rapid export growth to the U.S., while also increasing their exports to China.

Mexico's annual exports to the U.S. have roughly doubled since 2008 to more than $400 billion, and they have increased to China, too. At the same time, China has picked up a growing share of trade from Russia, as Europe shifts away from engagement with its eastern neighbor, and China's exports to Southeast Asia are rising.

The pathways of finance are similarly shifting. U.S. cross-border loans peaked in 2011, flattened for several years and started growing again around 2016. Among the biggest recipients of increased U.S. lending are traditional allies in North America and Europe, including Canada, Mexico, France and Germany, evidence that old alliances are strengthening in a riskier world.

Southeast Asia is also gaining a growing share of U.S. foreign direct investment. China and Hong Kong accounted for 24% of all U.S. foreign direct investment into Asia in 2008, while Singapore accounted for 21%. By 2021, Singapore, a hub for investment in places such as Vietnam, Thailand and Malaysia, accounted for 38% of investment, while Hong Kong and China accounted for 26%.

A stressful landscape

The key question for business leaders, policy makers and workers is how to navigate a more costly and stress-inducing global landscape. Mr. Rodrik is skeptical that industrial policies to boost manufacturing in advanced economies will deliver many benefits to workers, because many of these economies are already service-oriented and unlikely to reverse that emphasis.

His bigger worry is that this new landscape is fraught with the potential for miscalculation, in which economic friction between countries leads to open conflict. The new globalization, he says, has already been weaponized by the use of tariffs, sanctions and export controls.

"The biggest threat is to peace and security," he says.

National-security concerns originally drove Google's planned Pacific Light Cable Network away from Hong Kong. Ted Osius, then a policy adviser at Google and former U.S. ambassador to Vietnam, remembers watching pro-democracy protests erupt in Hong Kong in 2019, and worrying about the risks of proceeding with billions of dollars of investment in a cable network there.

"No one knew what would happen to Hong Kong in the future," he says.

That year, the U.S. Justice Department, which leads the multiagency "Team Telecom" panel that reviews telecommunications matters, signaled its opposition to the project because of concerns over its Hong Kong partner, Pacific Light Data Communications Co., and the direct link to Hong Kong.

Google and Facebook, now called Meta Platforms Inc., were granted approval in late 2021 to land the cable in Taiwan and the Philippines. One new concern is whether Chinese tensions in Taiwan could jeopardize access to the cable there, too.

A spokeswoman for Google says the Taiwan node is licensed and operating and the firm is committed to its operations there. "Google's systems are designed for security and reliability on a global scale," she says. Meta's line to Luzon, Philippines is also operating and it plans new lines through the Java Sea to Singapore, emphasizing diversification.

The Hong Kong piece is not operating. The share price of Dr. Peng Telecom & Media Group, the Beijing-based controlling shareholder of the Hong Kong partner, has dropped more than 90% since 2015. The company did not respond to a request for comment.

Mr. Osius has since left Google to become chief executive of the US-ASEAN Business Council, a trade group that advocates for U.S. businesses in Southeast Asian countries such as Vietnam, Cambodia, Thailand, Malaysia and Indonesia. He says business is booming as companies look to diversify.

"U.S. business had too many eggs in the China basket," he says.

The biggest beneficiary in recent years has been another country under Communist Party rule: Vietnam. As in China, human-rights groups call out the Vietnamese government's repression of speech, religion and association. Also like China a generation ago, Vietnam's population of about 100 million people is young, growing, well-educated and motivated for economic advancement.

David Lewis, chief executive of Houston-based **ECV Holdings**, says the comparisons between China and Vietnam end there. Vietnamese leaders aim to be neutral in global politics, he says. Their focus is on growth, prosperity and inviting foreign direct investment. "What you have in Vietnam is everything we wanted in China, minus ambitions for world dominance," Mr. Lewis says.

His company seeks to build a power plant to fuel industrial parks around Ho Chi Minh City. The plant will be supplied largely by liquid natural gas imports from the U.S. Mr. Lewis says that Vietnam is restrained from tapping natural-gas reserves along the vast South China Sea coastline around it because of China's claims to that area. "Vietnam is not interested in picking fights," he says.

Shifting production

Japanese companies are getting into the global diversification game as well.

Matsuoka Corp. manufactures clothes on behalf of other brands, about 70% of which are for **Fast Retailing** Co.'s Uniqlo. In a business plan released in May 2022, the company said it intended to produce 71% of its output in Southeast Asia in the year ending March 2026, up from 50% in the year ended March 2022, largely by shifting production out of China.

As part of that plan, the company is investing 8.7 billion yen, equivalent to $65 million, to build new factories in Bangladesh and Vietnam in the two years ending March 2023.

"China's technical capabilities are high, but labor costs have risen, and it has become difficult to secure workers," a spokeswoman says. "In Vietnam and Bangladesh, it's easy to recruit workers."

The spokeswoman, who asked not to be identified, says the company has also become more attuned to the risks of operating in China, mentioning Covid-related lockdowns last year as an example of such risk.

China accounted for 74% of Japan's textile imports in 2012, a figure that fell to 58.7% in 2021, according to the Japan Textile Importers Association.

During Covid, many companies were focused mostly on survival. With Covid receding, the long run is now coming into focus, says Jake Siewert, head of political-risk oversight at Warburg Pincus, a U.S. investment firm, and former official in President Barack Obama's White House.

Reglobalization, he says, is still in its early stages. "These supply chains were built over 30 years or more," he says. "The idea that they're going to completely unravel overnight is crazy."

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Trade's Rise—and Decline

World trade as a share of world GDP estimates

70% / 60 / 50 / 40 / 30 / 20 / 10 / 0 — 1870 / 1900 / 2000

Sources: Mariko Klasing and Petros Milionis, 'Quantifying the evolution of world trade, 1870-1949' (pre-1950 estimates); Penn World Tables (1950-2015); World Bank (after 2015)

Financial Shifts

Loans by U.S. banks to borrowers in selected nations show renewed strength of old alliances

$500 billion / 400 / 300 / 200 / 100 / 0 — 2000 / '05 / '10 / '15 / '20

Canada and Mexico
France and Germany
Hong Kong and China

Source: Bank for International Settlements

China Slide

Share of U.S. imports. Supply-chain shifts since the 2018 Trump tariffs and the Covid pandemic have cut into China's numbers.*

Percent of U.S. goods imports by nation

22.5% / 20.0 / 17.5 / 15.0 / 12.5 / 10.0 / 7.5 — 2000 / '05 / '10 / '15 / '20

European Union† / China / Mexico / Canada

*2022 data through November †European Union reflects current members plus U.K.
Source: Census Bureau

Asian Growth

Vietnam, India and Taiwan are among Asian nations gaining share of goods imported to the U.S.*

Vietnam / South Korea / Taiwan / India / Thailand / Malaysia

Percent of U.S. goods imports by nation

4% / 3 / 2 / 1 / 0 — 2000 / '05 / '10 / '15 / '20

*2022 data through November
Source: Census Bureau

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Oil Prices Are Seen Staying Steady This Year—With a Couple of Big Ifs

The big unknowns: How much oil will China consume, and how cautious will U.S. frackers be?

BY COLLIN EATON AND BENOÎT MORENNE

OIL PRICES generally aren't expected to change dramatically this year, but two big questions loom over that outlook: Will China have the workers needed to rev up its economy as the country loosens its Covid restrictions? And will American energy companies focused on fracking stick to their recent reluctance to bankroll another expensive oil boom?

Brent, the international oil standard, peaked above $127 a barrel last year but has since tumbled, trading around $84 a barrel Thursday. Around two-thirds of energy executives surveyed by the Federal Reserve Bank of Dallas late last year expected West Texas Intermediate oil prices—which tend to fluctuate a few dollars a barrel below Brent—to end 2023 between $70 and $90 per barrel. The forecast is based largely on the fact that analysts expect global oil supply to outpace demand this year as economic growth slows.

The biggest wild card for oil prices is China. Analysts at Bank of America Corp. expect China's economy, emerging from Covid-19 restrictions, will add 700,000 barrels a day to global growth in oil demand this year. But uncertainty surrounding the trajectory of Covid cases in China could affect the country's economic rebound, they say.

Robert Yawger, executive director for energy futures at Mizuho Securities, says a surge of Covid-19 cases in China would curb demand for crude there, because without enough workers, "you can't start industry up."

That could push oil prices down below consensus expectations. But uncertainty about China cuts both ways. Several analysts have said oil prices could shoot higher than generally expected, perhaps well above $100 a barrel, if the reopening of China's economy produces unexpectedly strong growth.

U.S. output

Then there's the question of the American shale industry's plans.

U.S. energy companies that rely primarily on fracking—which account for nearly two-thirds of U.S. oil output—are maintaining a cautious approach to start 2023, pledging not to overspend in an effort to ramp up production and focus instead on maximizing profits. It's a strategy they began following in response to shareholders imploring the companies to cut back spending in pursuit of growth.

The changed approach has helped restrain the country's oil production. Many analysts initially projected growth of a million barrels a day or more in 2022 for U.S. oil output. But last year's output is now expected to have increased by less than 600,000 barrels a day, according to James West, a senior managing director at investment-banking firm Evercore ISI.

This year, output is again expected to increase much less than in the past decade's boom years. American oil production is expected to increase about 680,000 barrels a day this year, according to the Energy Information Administration's latest outlook—less than the increase of about 1.1 million barrels a day the EIA forecast for 2023 early last year. In its latest forecast the EIA revised its estimate of output for December 2022 down significantly because of the impact of unusually severe weather that month.

If the U.S. shale industry continues to restrain spending on production growth, that would put upward pressure on prices, or at least fail to counter any price increases that could arise from other factors such as a surge in demand from China.

Industry commitment

Some investors question whether the industry will stay committed to budgetary discipline in the wake of sustained high oil prices. But there are several reasons a turnabout is unlikely. For one, the resistance to production increases is now ingrained in executive-compensation plans that give priority to shareholder returns over increased drilling.

Energy Rally

The S&P Energy index has jumped about 60% since the start of 2022

Source: S&P Dow Jones Indices

Production is also being limited by elevated costs of labor, manufactured equipment and raw material such as steel. In addition, some oil executives have warned that companies are running through their top-quality well locations quickly, another reason not to increase output. "Companies realize inventories are finite," says Steven Pruett, chief executive of Elevation Resources LLC, a producer operating in the Permian basin of West Texas and New Mexico.

Spending by oil companies in the U.S. is expected to rise about 20% this year. But that increase is largely due to cost inflation, not greater investment in production, says David Deckelbaum, an analyst at Cowen & Co.

U.S. oil producers have profited from their focus on cost-cutting rather than production increases. The top 10 independent U.S. oil producers collected a combined $19 billion in free cash flow in the third quarter of 2022, according to FactSet, up from about $12 billion for the same period in 2021. Several U.S. oil producers saw record quarterly cash generation last year.

Despite that profitability, many investors are still wary of plowing money into shale companies, says Matt Stephani, president of investment adviser Cavanal Hill Investment Management. After years of losses during the industry's earlier pursuit of rapid growth, investors are still feeling out whether the industry is a safe bet, Mr. Stephani says. "There's still some skepticism."

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$19 billion
The amount of cash, after capital expenditures, generated by the top 10 independent U.S. oil producers in the third quarter of 2022

3.1%
The projected increase in daily U.S. oil production from year-end 2022 to year-end 2023, according to the Energy Information Administration

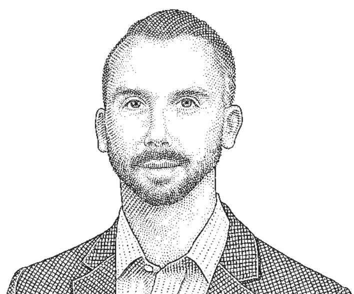
$80-$90
The per-barrel oil price that nearly 45% of U.S. oil executives expect by the end of 2023, according to a recent survey by the Dallas Fed

10%
Exxon Mobil's expected growth in oil production this year and beyond in the Permian Basin, the top U.S. oil field, down from about 20% in 2022 and 25% in 2021

JOE RAEDLE/GETTY IMAGES

A pump jack in Odessa, Texas, pulls oil from the Permian basin. U.S. producers are expected to raise output moderately this year.

ON THE CLOCK | CALLUM BORCHERS



Workers, Get Ready for a Return to Normal. Call It the Great Rebalancing.

This may be the year when employer-employee power dynamics gets back to more familiar terrain

AMERICAN workers' wild ride is coming to an end.

After three whiplash-inducing years of, first, professional vulnerability and, then, perceived invincibility, many people are returning to more typical levels of career security and leverage.

Call it the Great Rebalancing of the employer-employee relationship.

"We're clearly headed there," says Heidi Shierholz, president of the Economic Policy Institute.

Not long ago, at the pandemic's onset, things were so bad that people lost jobs in record numbers as the U.S. unemployment rate reached 14.7%.

Then things got so good that workers resigned in record numbers. There was a catchy name for this trend, I believe.

Adding to the volatility, savings swelled and shriveled with the stock market, causing some people to lurch between hope for an early retirement and fear of working forever. Raises that made some feel flush were offset by inflation, in many cases.

The "quiet quitters" who reduced their on-the-job efforts while feeling untouchable last year may now be angling to fill key roles when their companies freeze or cut head counts.

Ms. Shierholz says that workers are still in good shape, overall, but certain key metrics are trending down toward normal ranges. December's hourly earnings increase of 4.6% from a year earlier was the smallest rise since mid-2021, and the 223,000 additional jobs were the fewest per month in two years.

To complain about such decreases would be akin to griping if Yankees slugger Aaron Judge were to hit only 50 home runs this year, after smacking an American League-record 62 last season. It's unrealistic to expect new peaks all the time, and it's worth remembering what 2020 was like. (Mr. Judge, beset by injuries, hit 9 homers that year, by the way.)

Francesco Carucci, a California software developer, says he knew that his pay package was "wildly inflated" when he joined Meta Platforms Inc. last January. He says Facebook's parent company tripled the total compensation that he earned at his previous employer, amid a hiring spree in a historically tight labor market.

Then Meta laid off Mr. Carucci late last year in a round of 11,000 job cuts. Being aware of his bloated comp didn't dull the sting of losing it, he says, and he got an additional reality check this month when he accepted an offer that is worth half of the one he received a year ago.

Still, he says his new pay is reasonable—more than what he made a few years ago—and the interview and negotiation process was more in line with what he has usually experienced over a 25-year career. He adds that he's trying not to take the layoff personally. He views it instead as part of a natural and inevitable correction to the job market.

Others would do well to practice the same attitude. Andy Challenger, senior vice president of Challenger, Gray & Christmas, which helps companies manage layoffs and provides career coaching to the dismissed, tells me that business is picking back up after two of the slowest years in the firm's history.

He offers a blunt translation of what that means: "We know that there are a lot more layoffs coming."

Ominous as that sounds, Mr. Challenger says the prospects of finding new work are generally good. Job openings, while shrinking, still outnumber the unemployed by several million, according to federal data. He expects that gap to narrow as the year goes on and advises job seekers to redouble their urgency.

"It's not a time to lay back and feel too comfortable about the tight labor market," he says. "Even if you're getting lots of messages from recruiters today, that can dry up pretty quickly as things turn."

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A floating terminal for natural-gas tankers in Wilhelmshaven, Germany, is part of efforts to replace Russian supplies.

SINA SCHULDT/DPA/ASSOCIATED PRESS

Governments Push Deeper Into Energy Markets

Energy security became paramount following Russia's invasion of Ukraine, prompting governments to take aggressive steps to shore up supplies and tamp down prices

BY PHRED DVORAK

GOVERNMENTS are stepping into the energy markets in a way the world hasn't seen in decades, propelled by a tug of war over oil and natural gas and a heightened sense of urgency on energy security.

Russia's war on Ukraine and the resulting turmoil in fossil-fuel markets has been a major factor in the interventionism, prompting countries to shore up supplies, tackle soaring prices and rethink where they get their energy.

In Europe, where fuel shortages and price shocks have been particularly acute, Germany and France have moved to nationalize big energy companies that were facing huge losses, while the European Union is rolling out a cap on the price of natural gas.

The U.S. has released millions of barrels of oil from its strategic reserves in an attempt to reduce gasoline prices, used emergency powers to bolster the import of solar panels and unleashed a torrent of measures to help create domestic supply chains for clean energy.

Last month, the EU and the Group of Seven advanced democracies said they would try to prevent Russian crude oil from selling at a price higher than $60 a barrel. Russia has retaliated by refusing to sell its oil and petroleum products to those countries.

Such steps have already exacerbated uncertainty in markets and roiled relations between countries. The trend is likely to intensify in 2023 and beyond, energy experts say.

"Government is back in the energy business in a big way," says Daniel Yergin, vice chairman of S&P Global and a longtime chronicler of energy trends.

A guiding hand

Government intervention in energy markets isn't new. In the West, the pendulum tends to swing between less meddling when fuel supplies are stable and more during times of stress. The latest period of heavy intrusion was during the 1970s, when disruptions to the supply of oil from the Middle East sent prices soaring and left drivers in the U.S. and other countries in long lines for gasoline, energy analysts say.

The current surge in activism was also spurred by fuel shortages and skyrocketing prices, after the fallout from Russia's invasion of Ukraine further squeezed supplies that were already strained by years of underinvestment, the analysts say.

This time, the shocks to the global energy system are even greater than they were in the 1970s, since they are affecting not just oil markets but other energy sources such as natural gas, coal and uranium, says Mr. Yergin.

Before the invasion, Europe imported around 40% of its gas and 30% of its oil and refined products such as diesel from Russia. Between European sanctions and Russian moves to reduce exports, those percentages will likely dwindle to the single digits this year.

The stress of supply crunches is being compounded by geopolitics, as the U.S., Europe and their allies pull away from Russia and its fuel exports, while China, India and others lean in. Heightened energy-security concerns and the attraction of new, lucrative markets are prompting governments to play a bigger role in industries such as solar or wind too.

"The whole map of global trade and energy is being redrawn for traditional oil and gas," says Jason Bordoff, founding director of the Center on Global Energy Policy at Columbia University. At the same time, "new clean-energy sources are coming into the global market and...countries are trying to intervene in markets to affect where those get developed," he says.

Cost and supply

Much of what governments are doing is aimed at curbing high fuel prices and fending off shortages, moves that in some cases have helped countries secure badly needed supplies and head off economic damage.

German officials say the government's takeover of utility Uniper SE, which was struggling with massive losses from purchases of natural gas at soaring prices, has helped keep the country's energy system stable. In the U.S., solar-industry executives credit moves by the Biden administration with easing some of the squeeze on panel supplies.

But some analysts warn that intervening in the markets could have the opposite effect.

"Government intervention in these kinds of markets is a two-way sword," says Joseph Majkut, director of the energy-security and climate-change program at the Center for Strategic and International Studies. "Things can happen that are unintended."

'The whole map of global trade and energy is being redrawn for traditional oil and gas.'

—Jason Bordoff, Center on Global Energy Policy

Take Europe's gas-price cap, the goal of which is to prevent a disastrous increase like last summer's, when supply disruptions at a major gas pipeline from Russia helped push prices to a new high, pummeling businesses and the economy. The cap could result in supply heading to places like Asia instead of Europe, potentially worsening shortages on the continent, said an October report from the U.K.-based Oxford Institute for Energy Studies.

"Political intervention remains one of the biggest risks faced by the energy industry and has the long-term effect of reducing confidence," the European Federation of Energy Traders said in a response to the EU's decision to implement the cap at the end of December.

Some natural-gas traders have already trimmed positions in Europe out of fear that the markets will get less liquid and more volatile, says Yan Qin, a lead analyst at data provider Refinitiv.

How much power?

Some energy analysts say that there are limits to governments' ability to sway global markets, and that concerns over intervention may be overblown. The U.S., for instance, is urging its oil-and-gas companies to produce more, but it doesn't control what they ultimately do, says Dan Klein, S&P Global Commodity Insights' head of energy pathways. The data provider is predicting that prices in most energy markets will likely be lower this year than in 2022, he says.

Warm weather recently in the U.S. and Europe has pushed natural-gas prices down to levels last seen before the war in Ukraine, while much Russian oil has been trading below the G-7's $60 price cap, largely on sales to countries such as China and India that aren't implementing the cap.

Still, many energy experts say the effects of more-muscular government energy policies are rippling through the industry in other ways, changing money flows and stressing relations between countries.

Investors are pouring money into clean-energy projects in the U.S.—sometimes pivoting from projects in other countries—attracted by generous tax incentives and other subsidies Congress rolled out last year. That has raised hackles in Europe and Asia, particularly among car makers upset at rules that could give beefier tax credits for electric vehicles whose components were made in the U.S.

Last month, the U.S. delayed releasing the details of those rules following strong protests from some of its allies.

"Alliances that we have today are under more strain" in today's energy landscape, says Kevin Book, managing director of Washington, D.C.-based research firm ClearView Energy Partners LLC.

DOUG CHAYKA

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The Anxious Global Consumer: By the Numbers

BY RACHEL WOLFE

Shrinking real wages, a slowing job market and pressure on retirement savings have many people feeling gloomy. Slowing inflation may brighten the outlook.

MANY consumers around the world see an economic downturn coming in the year ahead.

U.S. consumer sentiment reached an all-time low in June 2022 and remains 15% below where it was a year ago, according to the University of Michigan. Expectations also took historic dips over the past year and remain depressed in Europe and China, according to TradingEconomics data from the European Commission and National Bureau of Statistics of China.

People feel uncertain about their own and their country's financial futures due to such factors as stubbornly high energy and food prices, the war in Ukraine and lingering Covid-19 disruptions, says Joanne Hsu, director of the Surveys of Consumers at the University of Michigan.

The relatively strong global labor market over the past few years has allowed people to keep spending, economists say, though many predict employment will contract in the coming months. One bright spot: Inflation appears to be easing in some of the world's largest economies.

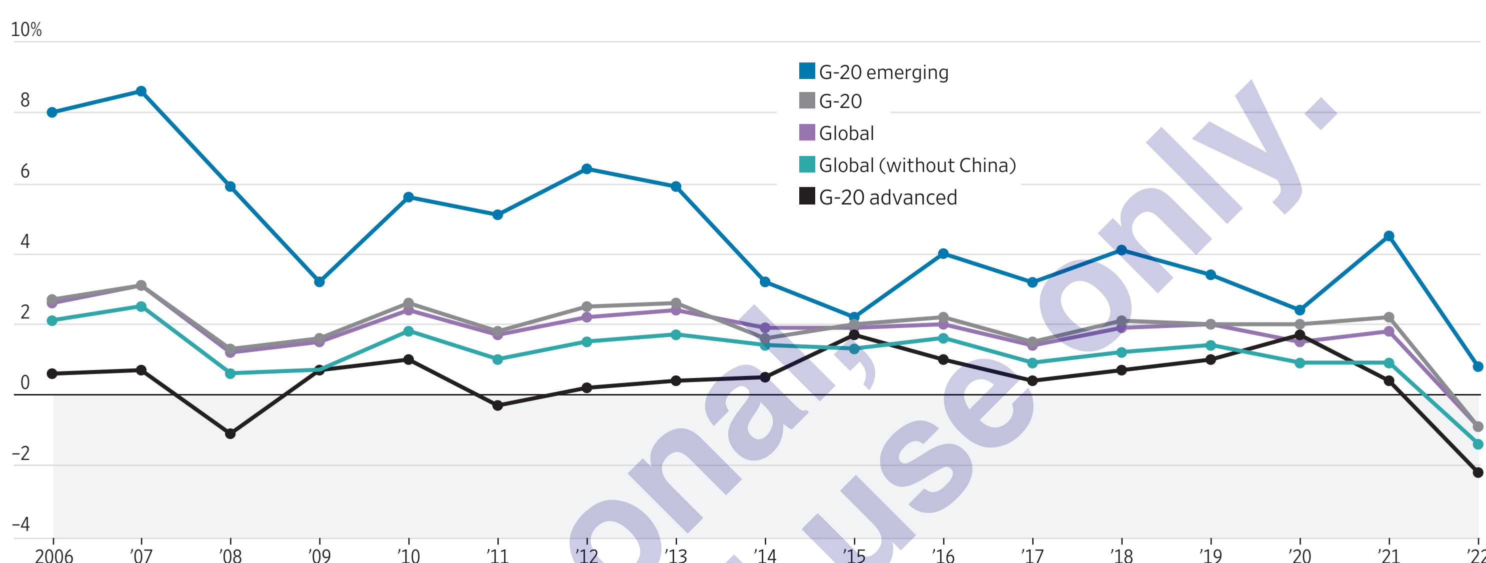
There is no widely referenced universal survey of consumer sentiment around the world, but the following data on monthly wage growth, unemployment, wealth and retirement, and inflation help paint a picture of an anxious global public.

Ms. Wolfe is a Wall Street Journal reporter in New York. Email rachel.wolfe@wsj.com.

Real wage growth dropped

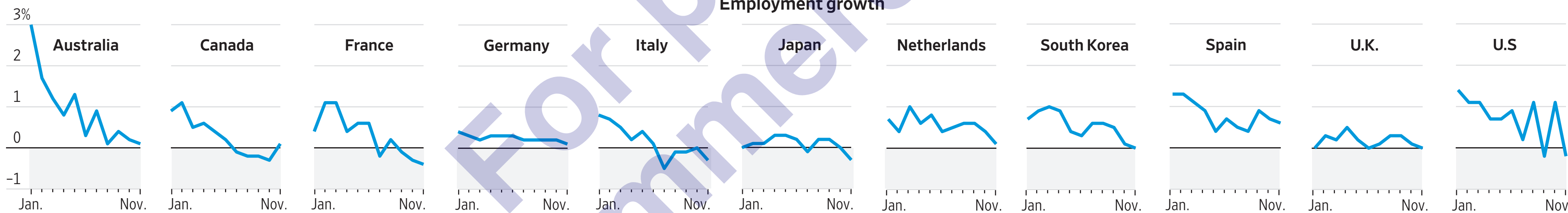
Inflation has caused consumer purchasing power to plummet, according to a November 2022 report from the International Labour Organization. Although nominal wages increased in many countries, they did not keep up with inflation.

Real global monthly wages, including China, fell 0.9% in the first half of 2022, the ILO says. That was the first time this century that real (inflation-adjusted) global wages have fallen. Without China, global monthly wages were down 1.4%. Among advanced G-20 countries, including the U.S. and U.K., real wages declined an estimated 2.2%, while real wages in emerging G-20 countries grew by 0.8%, 2.6 percentage points less than in 2019. Rising inflation has had the biggest cost-of-living impact on lower-income earners, ILO research officer Rosalia Vazquez-Alvarez says.



The job market is slowing

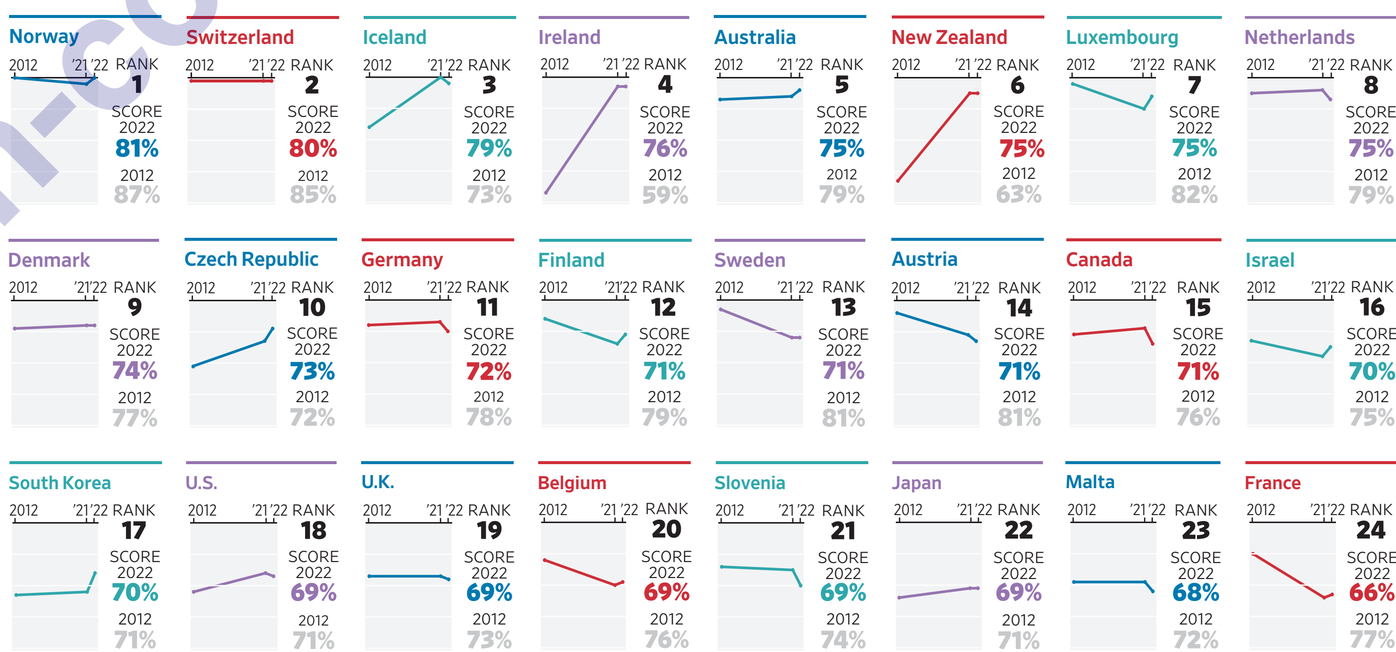
We're at the start of a downturn in the labor market, a new report from Oxford Economics suggests. The study—which tracked whether the word "job" and other labor-market terms were referred to positively or negatively across 400,000 sources in 123 languages—finds that sentiment is coming down quickly in countries around the world, especially in Europe. "Most of the lines here are pointing downwards now," says Innes McFee, the report's co-author and chief global economist at Oxford. Mr. McFee says the labor market might be starting to feel the impact of the central banks raising rates.



Retiring is becoming more difficult

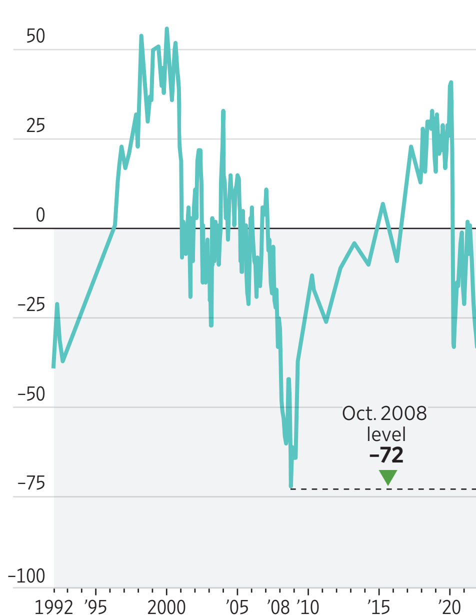
Last year marked one of the worst to retire in recent memory, according to the Natixis Center for Investor Insight's annual Global Retirement Index. Almost every developed country is finding the challenge of ensuring a secure retirement for their citizens greater than a year ago, executive director Dave Goodsell says. Global Retirement Index scores, shown here, are relative to how well a country performs compared to others in the index. Each country's score is based on how well retirees can answer four questions: "Can I afford to live in retirement? Will I have access to the quality healthcare I need? Will the economy be supportive of my retirement? Will I live in a healthy environment?" Many country's scores have declined, which Mr. Goodsell attributes to inflation forcing people to spend down their savings more quickly, and the rapidly aging population in the developed world.

Note: Natixis calculates Global Retirement Index rankings for countries based on how retirees' rate their access to quality financial services, robust healthcare, a clean and safe place to live and other factors. Percentage scores are overall scores out of 100 indicating how well a country performs compared with others in the index.



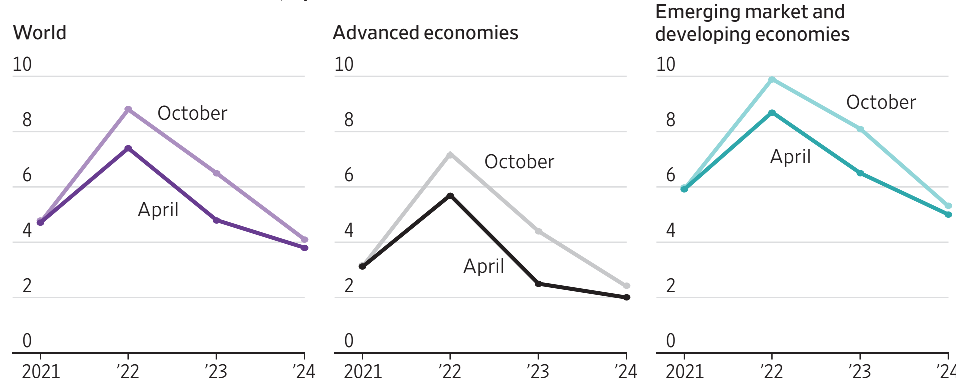
American economic confidence remains low

Gallup has been measuring the American public's faith in the economy since 1992. Average confidence over the past 20 years has been close to zero, reflecting roughly equal periods of positive and negative scores over the three decades of measurement. As of November, confidence was at minus 39. "That is what I would call in profoundly negative territory," says Lydia Saad, Gallup's director of U.S. social research. That number is in the bottom 10% of the firm's monthly readings since 2001 and reflects the 55% of Americans who said they had experienced financial hardship because of rising prices as of December, Ms. Saad says. The index had been as low as minus 58 in June and Americans continue to be less confident about the economy now than they were in 2021 and early 2022.



Inflation is beginning to slow

Despite all this, inflation appears to be slowing. If that continues in 2023, some of the economic pressure might dissipate and real wages could rise. In December, the U.S. consumer-price index was up 6.4% from a year earlier, compared with a 9% increase in June. Gasoline prices in the U.S. have fallen in recent months, though groceries remain stubbornly expensive and energy bills are still a concern, especially in Europe as a result of the war in Ukraine.



*Wage growth for 2022 was estimated by comparing the first two quarters of 2022 with the corresponding period in 2021. The G-20 comprises Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, Mexico, Russia, Saudi Arabia, South Africa, South Korea, Turkey, the U.K., the U.S. and the EU.

Sources: International Labour Organization estimates based on official national sources (wages); Oxford Economics/Penta (unemployment); Natixis Investment Managers and CoreData research (retirement); Gallup (confidence); International Monetary Fund (inflation)

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OLIVER BURSTON

KEYWORDS | CHRISTOPHER MIMS

Central-Bank Digital Currencies Are Coming—Whether Countries Are Ready or Not

The development could have a profound impact on the banking system. But few people understand it.

"CENTRAL-BANK digital currency" doesn't exactly roll off the tongue. But you might want to get used to saying it. These so-called CBDCs, or digital versions of dollars, yuan, euros, yen or any other currency, are coming, say those who study them. And depending on how they are designed and rolled out, their impact on the banking system could be profound.

One hundred and fourteen countries are exploring digital currencies, and their collective economies represent more than 95% of the world's GDP, according to the Atlantic Council's Central Bank Digital Currency tracker. Some countries, including China, India, Nigeria and the Bahamas, have already rolled out digital currencies. Others, like Sweden and Japan, are preparing for possible rollouts. The U.S. is studying the issue and has run trials of various technologies to enable a digital currency, although Fed chair Jerome Powell has indicated the U.S. central bank has no plans to create one, and won't do so without direction from Congress.

Debates about the necessity, utility and potential pros and cons of digital currencies are often confusing, and confused, in part because every country rolling out a digital currency is doing it in its own way.

Generally, however, CBDCs can be roughly divided into two types: those designed for use by financial institutions and those designed for use by the general public.

Old vs. new

The first type is just a new way for central banks to transfer money to commercial banks.

More specifically, some central banks are testing whether money transfers between financial institutions—which in some cases can take days to settle—might be made safer and more efficient under a system in which central-bank money is represented by digital tokens and transactions are settled on a shared distributed ledger, concepts borrowed from cryptocurrency and blockchains. One such system is being tested by the New York Fed and a range of big U.S. banks and financial institutions.

The second type of CBDC is a digital version of fiat money made available to the general public through accounts held by a central bank or a commercial bank. From the perspective of a regular person or business, this kind of CBDC isn't any different from the electronic money in their bank accounts today—it's just a digital dollar. What makes these kinds of CBDCs special is that they are created, and held, in accounts that a central bank has direct access to. If another pandemic happened, for example, the Fed could just deposit stimulus "checks" into every U.S. citizen's digital-currency account.

This type of CBDC represents a departure from the way money is created and distributed today, in that everyday people would now have accounts, or "wallets" that contain money created by their country's central bank itself, instead of by their commercial bank. It represents a profound shift for central banks, from their traditional role as providers of money to a country's banking and financial system, to connecting directly with everyday people.

China's digital yuan is one such currency, and it can be used by everyday Chinese people through existing, and very popular, digital payment services like Alipay and WeChat Pay. India's digital rupee is an equally bold experiment in allowing the country's citizens to transact with a digital version of their currency in a way that could bypass traditional banks.

Question of control

At this point, the average person is probably wondering why, in a world in which billions of people have become accustomed to paying for things with electronic payment systems already, anyone needs a digital version of their currency.

The answer to that question depends on the motivations of the central banker, analyst or academic you ask. Many who study digital currencies argue that at the most basic level, a digital currency is all about control. The rise of cryptocurrencies—which are another form of digital money, but one that isn't controlled by a government or other central authority—and the potential of one nation's digital currency to eat away at the dominance of others' has driven interest in official digital currencies.

"There's a worry that if we don't launch a digital currency in the U.S. or Europe, China will set all the standards for them, and then we'll be at a disadvantage," says Megan Greene, global chief economist at the risk and financial advisory firm Kroll. "Also, digital currencies like crypto really scared the bejeezus out of central bankers."

What central bankers and other interested parties—like the Biden White House, which in a September report outlined the possibilities of a digital U.S. dollar—fear is the potential of cryptocurrencies to wrest control of the creation and transfer of money from central banks, leaving them without the tools they currently have for preventing their respective economies from running too hot or too cold.

> **114**
> countries are exploring digital currencies
>
> **>95%**
> The share of global GDP that those 114 countries represent
>
> Source: Atlantic Council Central Bank Digital Currency tracker

All of these threats remain entirely hypothetical for now, says Eswar Prasad, an economist at Cornell University. In his book "The Future of Money," he outlines the other reasons that policy makers give for wanting to create digital currencies.

Perhaps the most noble of those reasons is financial inclusion. In the U.S., only about 5% of people don't have a bank account. But in other countries, such as the Bahamas, which was the first country in the world to implement a digital currency, the figure is much higher—around 18%, according to the country's central bank. If everyone had access to an account with their country's central bank, and could use it to transact instantaneously with others using a digital currency, for a minimal or no fee, the idea is that it would bring many more people into the regional and even global financial system, with all the benefits that attend.

Less privacy

On the other hand, the potential downsides of a digital currency, even one initially intended for only the most benign purposes, could be profound, says Dr. Prasad.

First, there is the obvious issue of privacy. A digital currency could allow governments to track every transaction a person makes, no matter how minute. This level of transparency would be a powerful disincentive to using these currencies for crime or fraud, but it could also open the door to new kinds of social control, especially in countries with already-scant human-rights protections.

For example, says Dr. Prasad, a government could make it impossible to spend the digital currency on things the ruling party deems problematic, like alcohol or pornography. The government also could make transacting with certain people difficult or impossible—China already has a social credit system that ranks citizens algorithmically, and punishes them in various ways.

"Throughout history, I think you see many examples where you see tech that seems very benign get perverted into much more malign uses," says Dr. Prasad.

Even less-malign applications of digital currencies could lead to all sorts of unintended consequences. One, which the crypto industry has run afoul of many times in the recent past, is that the more complex and capable designers of a digital currency make their system, the greater the possibility that it could be manipulated in ways its designers didn't anticipate.

Set aside FTX, which appears to be a straightforward case of the misuse of depositors' funds. Set aside also the many hacks and thefts of cryptocurrency that have taken place of late. Plenty of crypto projects have failed or lost huge amounts of money even when they were functioning exactly as designed. The crypto exchange Mango Markets saw $114 million in funds siphoned out by a trader who didn't break any of the rules of the exchange, and simply exploited a feature of the behavior of the exchange that its designers didn't anticipate.

Then there are the failures of various "algorithmic stablecoins"—that is, cryptocurrencies that are supposed to be pegged to the U.S. dollar—which collapsed as soon as the overall value of cryptocurrencies was no longer rising.

Ironically, one of the biggest dangers of central-bank digital currencies could be that they succeed. Buried in the code and systems that dictate how they function could be a liability that a country doesn't discover until it's too late.

It's impossible to know what that liability might be, but the example of the many and varied experiments in new kinds of financial structures and products from the crypto industry should inspire designers of more-complicated digital currencies to tread carefully.

"I think it is inevitable there will be unintended consequences as a result of CBDCs," says Ms. Greene. "The Fed and the Bank of England are moving pretty slowly on digital currencies, which has made them the subject of criticism—but I actually think it is smart they're being methodical, because there are so many different decisions they have to make."

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The Big Technology Companies Prepare for a Difficult Year

They may have to deal with competitors, regulators and an economic slowdown

BY SAM SCHECHNER

A NEWLY humbled cadre of globe-spanning tech giants are about to see their resilience tested.

For years, the biggest tech companies have been lauded by investors—and at times assailed by smaller rivals and investigated by regulators—for how they appeared to be unstoppable juggernauts. Competitors, big fines and even a global recession brought on by the Covid-19 pandemic didn't stop revenue and profit from going up.

Now the tide has turned.

Another recession is looming. Europe is starting to put teeth behind its efforts to be tech's global regulator. And new competitors and technologies are threatening some big companies' holds on their markets. On top of that, big tech companies were seduced during the pandemic into heavy investments in personnel and new products predicated on the idea that the shift to virtual life would be enduring—something that hasn't panned out.

In response, big tech companies are retrenching, cutting expenses faster than they have in decades in an effort to navigate what tech executives and even bullish investors say is likely to be a tough 2023.

On Jan. 5, **Amazon.com** Inc. said its layoffs would affect some 18,000 employees. **Meta Platforms** Inc. said it would cut 13% of its workforce, or around 11,000 people. Google parent **Alphabet** Inc. on Jan 11 announced staff reductions of 15% at its healthcare unit Verily. Collectively, employers in the tech sector cut more than 170,000 jobs in the past year, based on estimates from Layoffs.fyi, which tracks media reports and company announcements.

"They've proven they can thrive in the go-go times, but the free-money era is gone," says Dan Ives, an analyst for Wedbush Securities, adding that he thinks big tech companies will ultimately navigate their troubles—which he calls a Category 5 storm—and stage a rebound. "Tech companies have spent like 1980s rock stars. Now they're starting to spend like senior citizens on a fixed budget."

No easy road

The economic factors behind the pivot to austerity are several, analysts say. Quickening inflation has led to higher interest rates. Russia's invasion of Ukraine has put new focus on supply-chain bottlenecks. And a recession would further damp demand—hitting advertising revenue that sustains some big tech companies, as well as consumer spending on electronics and others.

The new attitude comes as competition for big tech companies is becoming tougher—at least in some segments.

Google and Meta saw their share of U.S. digital-ad spending last year fall below 50% for the first time since 2014 because they are growing more slowly than the rest of the market, according to research firm Insider Intelligence Inc. That is, in part, because Amazon and upstarts like **ByteDance** Ltd.'s TikTok have seen their share of digital ads grow. But video-streaming services are also taking a growing share—a trend that should accelerate the launch of ad-supported versions of **Netflix** Inc. and **Walt Disney** Co.'s Disney+.

Advances in artificial intelligence could also reorganize the digital playing field. The ChatGPT chatbot released last year, which can produce plausible-sounding answers to an array of questions, has been lauded by some industry observers as an eventual alternative to current search engines like Google, even though the program can sometimes make factual errors.

OpenAI, which makes the chatbot, among other tools, is currently in talks to sell existing shares in an offer that would value the company at around $29 billion, roughly double a prior offer completed in 2021, the Journal reported earlier this month.

These challenges are coming to a head at the same time that tech regulation, long an amorphous and looming threat largely ignored by investors, has started to take a significant bite, too. European Union regulators earlier this month struck down Meta's legal justification for its highly targeted ads. That is leaving the company scrambling for a way to keep showing ads targeted based on its Facebook and Instagram users' online activity in the bloc.

The EU is also starting to implement two other new laws it passed last year—over objections from big tech companies—aimed at ensuring they give more of an opening to smaller competitors, and forcing them to more heavily police content on their platforms.

Even though companies subject to the Digital Markets Act—the law focused on tech competition—won't be officially named until later this year, and its provisions won't be enforced until 2024, the law is already pushing companies to change their business practices. **Apple** Inc., for instance, is now preparing to let applications be downloaded onto iPhones and iPads outside its App Store, something the company had long said would compromise security, to comply with the law.

Amazon recently promised to give better treatment and prominence to third-party sellers in ways a company executive said were meant to comply with the new law, as part of its settlement of an antitrust lawsuit in Europe.

Other provisions of the law include a ban on a company with a search function giving priority in its results for its own products and tools over those from other companies—a provision that could require changes to how Google operates in the bloc—and a mandate that messaging apps from digital giants must allow smaller rivals to interoperate with them. That could cut into Apple's walled-garden approach to its Messages app on iPhones.

A change of tone

Big tech companies have been moderating their tone on regulation, saying they plan to comply with the new laws. "We're now hard at work exploring new processes and product changes to comply fully," a spokesman at Google says. "For us, it's key to keep a constructive, hands-on regulatory dialogue with the European Commission for many months to come."

Apple and Amazon declined to comment. A Meta spokesperson pointed to a statement from Mark Zuckerberg on a recent earnings call: "I believe the tougher prioritization, discipline and efficiency that we're driving across the organization will help us navigate the current environment and emerge an even stronger company."

What happens in the EU in the coming year could end up being a template for other parts of the world now considering legislation with some similar provisions, including the U.K. and India.

"The looming [Digital Markets Act] is already having an impact," says Anne Witt, a law professor at the EDHEC Business School's Augmented Law Institute, in Lille, France. "If the pressure piles up internationally, sooner or later it may make sense for these companies to align their behavior globally."

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A New U.S. Law Aims to Reduce Drug Prices. But First, It Might Raise Them.

Pharmaceutical companies could try to blunt the limits on future price increases

BY JARED S. HOPKINS

PHARMACEUTICAL companies are grappling with the arrival of sweeping new U.S. legislation meant to blunt drug prices.

The impact in 2023 may actually be higher drug prices.

President Biden last year signed into law the bill dubbed the Inflation Reduction Act, empowering Medicare, the country's biggest buyer of prescription drugs, to negotiate how much it pays for certain high-price therapies. Another provision set a cap on price increases that requires drugmakers to pay Medicare rebates on treatments whose prices rise by more than the rate of inflation. Jefferies Financial Group Inc. analysts estimate the legislation could reduce pharmaceutical-company revenue by about $40 billion through 2032.

Many details of the law are still being finalized, and negotiated prices on an initial 10 drugs won't take effect until 2026. But in the near term, the legislation is likely to spur a couple of drug pricing strategies, analysts say.

To blunt the impact of limits on future price increases, companies are likely to launch new drugs this year at higher prices than they would have before the law passed, analysts say. They're also likely to raise prices on existing drugs more than usual while high inflation gives them cover.

The Inflation Reduction Act's requirement for companies to pay rebates to the government when prices of their drugs in Medicare programs increase by more than the rate of inflation starts this year. From July 2019 to July 2020, prices for about half of the medicines covered by Medicare increased by more than the rate of inflation, according to the Kaiser Family Foundation. But that was before inflation surged.

"The industry clearly has to be sensitive to and thoughtful about increasing prices in light of inflation caps, but currently [inflation] is running at an abnormally high rate," says David Risinger, an analyst at SVB Securities LLC.

In addition, several other factors may help drive bigger price increases this year. They include the rising cost of business related to inflation, supply-chain issues, and research and development, as well as rebates that are paid to middlemen, Mr. Risinger says.

Some analysts say you can already see the impact of the new legislation. **Bristol-Myers Squibb** Co. launched a new autoimmune drug called Sotyktu in September, after the law passed, at an annual cost of about $75,000—much higher than some existing rival drugs in the market, Mr. Risinger notes. (Most patients don't pay manufacturers' list prices, which don't reflect rebates, discounts and insurance payments.)

Launch prices of new drugs rose an average of 20% annually in 2008-21.

$40 billion

Projected reduction in drug-company revenue over the next decade from the Inflation Reduction Act

Source: Jefferies Financial Group

A Bristol-Myers Squibb spokeswoman said the company's approach "has always been to price our medicines based on the value they deliver" and takes into account "healthcare systems' capacity to provide appropriate, rapid and sustainable access to patients," among other factors.

Higher launch prices are more likely for treatments of cancers and rare diseases where the law may restrict future price increases than in more-competitive areas like diabetes or immunology, according to consulting firm ZS Associates.

One of the most watched drugs may be the Alzheimer's treatment lecanemab, from **Eisai** Co. and **Biogen** Inc., which the FDA approved this month. Eisai said it would sell the drug at a price of $26,500 a year for the average patient. The Institute for Clinical and Economic Review, a nonprofit monitor of drug prices, had found a fair price would be in the range of $8,500 to $20,600 a year. Esai says it priced the drug below the company's estimate of the treatment's value to U.S. society of $37,600, "to promote broader patient access, reduce overall financial burden, and support health-system sustainability."

Launch prices already have been climbing sharply for years. From 2008 to 2021, launch prices for new drugs increased an average of 20% annually, according to a study by Harvard researchers funded by Arnold Ventures LLC and published last year in the Journal of the American Medical Association. In 2020-21, roughly half of new drugs carried list prices higher than $150,000 annually, the researchers found.

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