Dear Client:

To foreigners, the U.S. has increasing appeal for building or buying factories, firms and real estate. Look for a surge in foreign direct investment over the next five or six years, pushing annual inflow to $320 billion by 2018, nearly 50% higher than now. The U.S. share of foreign investment will grow after declining for over 10 years. It will represent a third of a $300-billion increase in total global investment.

Why? The fading allure of emerging economies such as China and India. Increasingly, they will be able to finance their own expansions, so returns won’t be as sweet for outside investors. Pay hikes for workers in China...15% a year. Production costs there are nearing parity with those of the U.S., which enjoys higher productivity rates. And a tarnished Europe. The cheap euro may make European assets look like bargains now, but long-term woes, including high labor costs and overburdened national budgets, will slow growth.

For the U.S., that means millions of new jobs and a healthy boost for the economy in coming years. Manufacturing will nab more than half of the increase in investment funding, with automaking and oil and gas processing leading the way. South Africa’s Sasol, for example, plans a $10-billion gas liquefaction plant in La. Others will likely follow, heeding the siren song of America’s shale gas deposits. Auto and auto parts makers, particularly those from Italy and South Korea, will increase their presence in the U.S. Italy’s Magneti Marelli plans a $54-million expansion in Tenn. France’s Michelin...a new tire factory in S.C. Also attracting big bucks: The chemical, pharmaceutical and food industries. Ditto, semiconductors...especially from Taiwan and South Korea.

Snagging the next-largest chunk of foreign bucks: Retailing and wholesaling, particularly gasoline distributors plus sellers of furniture, groceries and apparel. Count on more overseas-based cheap-chic clothing retailers to join Sweden’s H&M and Spain’s Zara in challenging the giant U.S. firms that still dominate this market. The recent wave of investment in banking and insurance will continue, too. Though the U.K. duo of Barclays and HSBC won’t expand quite as aggressively following recent scandals, the retail push by Canada’s TD Bank isn’t likely to slow. Engineering, entertainment, high-tech and oil field services will also appeal to foreign investors. Not much more interest in the U.S. hospitality market, though.

Another big draw: Real estate. Through at least 2018, foreign investment in residential properties will climb by 20% a year, with about half the buying in Calif. and Fla., where prices remain in the tank, and Texas and Ariz. Commercial property...especially apartment buildings...will see foreign buying rise by about 10% a year.
Meager job gains last month aren’t likely to improve over the rest of 2012. Sales of cars and homes are strong, but not strong enough to fuel growth in the rest of the economy. And uncertainty about the election and pending fiscal cliff will intensify managers’ caution, discouraging hiring. The average monthly net gain so far this year is a discouraging 139,000, even slower than last year’s job growth.

Odds are the Federal Reserve will try another round of quantitative easing... bond purchases, probably in the neighborhood of $75 billion to $100 billion a month. Little chance that the move will lift economic growth, though. Still, not acting could lead to further deterioration, a chance Chm. Ben Bernanke won’t want to take.

Regardless of whether Mitt Romney or Barack Obama wins in the fall... Don’t expect big changes in the financial reform law named for its sponsors, ex-Sen. Chris Dodd (D-CT) and Rep. Barney Frank (D-MA). Romney, to be sure, disagrees with big chunks of the law designed to prevent the kinds of major problems that led to the financial mess in 2008, but he agrees with a handful of key provisions. Romney isn’t likely to call for full repeal, despite pressure from some GOPers. Instead, he’d push to reduce the burden on banks, requiring U.S. regulators to scrap an existing stricture whenever they implement a new one. He’d also move to loosen restrictions on bank investments in private equity funds and hedge funds. A top target of Romney cuts: The Consumer Financial Protection Bureau.

If he wins, look for his administration to change CFPB oversight from a single director to a commission structure, putting it on the same footing as other financial regulators. A second Obama term would leave rulemaking on its current trajectory.

Money market reform isn’t dead, but reaching agreement has been tough for the Securities and Exchange Comm. If consensus continues to elude the SEC, look for the Financial Stability Oversight Council to deem the $2.6-trillion industry systemically important and thus under its purview in the Washington hierarchy. SEC Chairman Mary Schapiro wants money market values to float, replacing the practice that shares trade at $1 despite minor moves in asset values. She’ll also push to require funds to hold more capital and restrict fund withdrawals to prevent market runs if values fall. So far, though, she doesn’t have the votes.

If Romney wins the White House, reform efforts will be doomed for sure. He’ll nominate a Republican to replace a Democrat whose term on the SEC expires.

As Apple’s iPads are incorporated into more and more U.S. classrooms... There’s huge potential for makers of education-related digital products and applications. This $600-billion piece of the economy will grow by 20% a year. Other tablet makers will share in the action, but as the dominant producer, Apple will get the most orders from schools and most of the attention from developers.

The shift to tablets will help schools save money and beef up performance in the classroom. After the initial investment, districts can easily update digital texts and teachers can create their own course content, especially as software improves.

One development tied to the growing use of smart phones and tablets: A shift in strategies for digital advertising to mobile-friendly approaches. Pop-ups and other ads common on computers irritate users of smaller devices. Advertisers will focus on sending content that is relevant to what a person is doing at the moment, not tailored to general browsing habits. And they’ll ask consumers for more information to help them craft personalized pitches for goods and services. For tablets... ads that turn into games or give a 3-D look at some products.

Changes for digital shopping in time for the holidays, too: Daily specials from specific companies. Incentives for customers who select items to purchase but don’t follow up to complete online transactions. Online-only deals. Free shipping.
**POLITICS**

Most scenarios for a Romney victory require him winning Fla., Ohio and Va. But Republicans are trying to create wiggle room by pushing hard in Wis., a state that hasn't gone for a GOP presidential hopeful since Ronald Reagan in 1984. It's a tough path, but so is running the table in the three big swing states. One plus for Romney: Running mate Paul Ryan calls Wis. home. Also, GOP Gov. Scott Walker easily survived a contentious recall effort earlier in the year, and ex-GOP Gov. Tommy Thompson is favored to snatch a Democratic Senate seat. The attention may not matter. President George W. Bush lost there in 2004, despite making Wis. a second-term target. He visited 12 times but fell by 11,800 votes.

**HEALTH**

Employers that receive rebates on health insurance premiums must act fast. In most cases, they have just three months to pass along employee shares. The rebates started going out in July from insurers that didn’t spend enough on care. Some companies are giving the full rebate to workers, either through cash payments or by cutting premiums...though firms can keep a share tied to the amount they pay. Visit [kiplinger.com/letterlinks/premiums](http://kiplinger.com/letterlinks/premiums) to view the complete set of rebate rules.

Meanwhile, many employers fret about a reinsurance fee set to start in 2014. The health law establishes a temporary program through 2016 to stabilize premiums when insurers factor in the cost of covering individuals with high-dollar claims. The fee hasn't been set yet, but estimates put it at $60 to $100 per person insured. The fees will be paid by insurers or administrators, but are likely to be passed on.

Another health issue for employers: Getting ready for an early flu season... starting in Oct. this year rather than Nov. Inoculating workers saves money... $70 per person in medical charges and lost productivity, much more than shots cost. Vaccine supplies are plentiful this year. A moderate flu season is expected, based on data from the Southern Hemisphere, where cases are winding down.

**MAIL DELIVERY**

Rural post offices have staved off a death sentence, but big changes are afoot: Reduced hours of operation and retailers becoming approved postal vendors, for starters. In time, the changes will save the U.S. Postal Service $500 million a year. The service cuts will allow the beleaguered USPS to put off starker choices to erase deficits, including eliminating Saturday delivery and closing some offices.

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**SENATE RACES**

Will Elizabeth Warren be a hero or a goat for Democrats this election year? The answer may determine which party rules the Senate starting in Jan. Warren is challenging Mass. GOP Sen. Scott Brown, who seeks a second term. The Bay State is tough terrain for any Republican, even a moderate incumbent, so national Democrats see the race as a solid opportunity to pick up a seat. If Warren wins the Mass. Senate race, the odds of a GOP majority are long. Republican gains in Neb. and Wis. will be partially offset by a loss in Maine. A Warren victory would mean Republicans need to capture four of six states from Democrats...Fla., Mont., Ohio, N.D., N.M. and Va...plus win the presidency. With Democrats ahead in Ohio and Fla. and close elsewhere, that’s a tall order.

Warren’s convention talk brought rave reviews. So why do Democrats sulk? Because she’s running a lackluster 2012 campaign and is likely to lose unless she starts listening to political professionals and changes her course. National party bosses want her to spend less time in Boston and Cambridge... she’s a law professor at Harvard...and more time reaching out to blue-collar voters and to local party leaders in rusty old mill towns who can help get out the vote. There’s time for a revival, but at this point a Warren win seems a stretch.

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We anticipate a bumpy ride for crude oil prices over the next few weeks. Oil markets are nervous, moving sharply on each new bit of economic data or any hint of a policy shift by central bankers, regardless of supply or demand. Sept. will be especially volatile because of anticipated announcements from the U.S. and European central banks of additional monetary easing measures. If those policies please markets, the recent run-up in crude prices will last a bit. But if the Federal Reserve and others stand pat, look for a short, sharp drop in prices. Longer term, global prices for crude oil will ease somewhat, but slowly, as several key fields reopen, bringing the supply more in line with demand. Look for a U.S. benchmark price of $85 to $90 per barrel by the end of the year.

Uncle Sam’s new fuel economy rules spell change for the auto industry. The latest standard, issued in Aug., takes effect with model year 2017 cars and gets stricter each year through 2025. The final target: 54.5 miles per gallon, vs. 31 now. As engineers wrestle with the daunting goals, keep in mind a few points: Figuring out the mileage rate gets complicated. The average shrinks to 49.6 mpg after factoring out credits the government will award to automakers for installing cleaner air conditioners in future cars. And the number falls further, to about 40 mpg, when converted to what motorists actually see on window stickers. Expect a big boost for alternative fuels. The rules award additional credits to manufacturers that produce cars and trucks that run on compressed natural gas, diesel, fuel cells or electric motors and batteries. Expect to see more of all of them. Cars will include parts made with lighter materials. Smaller engines, too. And they’ll come with fatter price tags...as much as $2,000 more in 2025, according to federal regulators, but $9,000 extra based on auto industry estimates.

Down the road...a solid year for car sales in 2013. And a big finish this year. Expect sales to hit 14.5 million or so by the end of 2012, as low interest rates on loans and the increasing age of cars on the road drive potential buyers to auto dealerships. Next year, look for sales to top 15 million...up from 12.8 million in 2011. How much above 15 million depends on the overall health of the U.S. economy. At a minimum, the unemployment rate must come down to keep sales motoring along.

Thinking about ditching cable TV? You have plenty of company in the U.S. By year-end, 3.6 million subscribers will have dropped cable since 2008, turning instead to online video streaming services or Internet-enabled televisions. The numbers will grow as new content is developed. The streaming giants... Netflix, Hulu and YouTube...are making big investments in original content. Also, Apple and Google will expand their efforts, and that's sure to attract new customers. But big cable companies will keep the upper hand, bundling offerings to appease 100 million households and charging competitors higher transmission fees.

Confusion about rules for in-flight use of electronic devices is about to end. The Federal Aviation Admin. aims to issue relaxed guidelines by late 2013, spelling out industrywide rules for when newer devices such as tablets may be used. The devices are allowed now if airlines can demonstrate that their radio signals don’t hurt operations or communications. But most carriers don’t pay to test devices, choosing instead to ban them or limit their use to gates or at certain points in flight. Don’t plan on calling from the clouds, though. Cell phones are still a no-no.

Yours very truly,

Sept. 7, 2012

THE KIPLINGER WASHINGTON EDITORS