

Strictly Confidential

CRYPTO TURNS TO TRADITIONAL

Monthly Report – July 2025



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TRACE: Crypto Turns to Traditional

"If I seem unduly clear to you, you must have misunderstood what I said." – Alan Greenspan

Theme: Frenzy of Crypto Cashing Out from Traditional Channels

(This piece might be controversial and is intended to be provocative.)

Back in 2017's year-end, the Bitcoin price fast approached USD 20k. On a dinner table in the grand opening of a friend's private club in Shenzhen, each took turns to comment on the meteoric rise. I was the only one without a single coin, same as today. When it was my turn, I offered a wide range, putting a floor of 5k due to consensus belief entrenched in enough people and a ceiling of 100k for the 21 million coins to have a market cap 1/10 (ballpark USD 2 trillion) the size of global underground economy on par with the US economy. The low since was 3.1k (down six-fold from 20k) and the high was 125k (up six-fold from 20k).

The crypto revolution has been one of the most extraordinary paper wealth-creation in modern history. From Bitcoin's genesis block in 2009 to the crypto market's valuation nearing \$4 trillion today, this ecosystem has conjured staggering value out of algorithmic consensus and collective belief. Yet beneath the surface of this technological marvel lies a series of existential questions about utility, regulation, and the uneasy symbiosis between crypto and traditional finance. This relationship may ultimately determine whether digital assets evolve into a sustainable parallel system or devolve into a speculative bubble with dangerous ties to mainstream markets, especially the booming tech sectors.

Bitcoin's foundational promise was decentralization, offering a trustless system outside traditional financial infrastructure. But after 15 years, the crypto world remains trapped in a paradox: its most valuable applications are those that tether it firmly to the very system it sought to replace. The industry's relentless search for purpose from smart contracts to NFTs to metaverse land grabs has collided with the reality that most blockchain "solutions" are answers in search of problems and hence repeatedly failed to provide real value.

Stablecoins, the latest pivot, claim to revolutionize cross-border payments by leveraging crypto rails for fiat transfers. But this supposed efficiency is a regulatory arbitrage, not a technological breakthrough. Stablecoins derive their speed from avoiding the compliance checks that bog down traditional banking, a loophole that regulators are rapidly closing. Their value is explicitly parasitic: one USDT or USDC equals one USD only because its issuer claims to hold equivalent reserves. Remove the dollar backing, and the edifice collapses.

China's financial system exposes this fallacy. Domestic bank transfers settle instantly, even for regulation approved transfers cross-border to Hong Kong. Alipay and WeChat Pay also handle billions of transactions daily without blockchain with instantaneous settlement. Janet Yellen once noted in 2021 that using Bitcoin for payments is "extremely inefficient".

Philosophically, decentralized crypto struggles with large-scale transactions due to inherent mathematical and structural flaws. Centralized systems scale linearly ($O(N)$), while blockchains face quadratic costs ($O(N^2)$), even optimized solutions only reach $O(N \log N)$. Trustlessness, a proud feature of blockchain, creates another barrier: no recourse for fraud, making irreversible transactions risky for high-value dealings. The result? Crypto works best only for medium-sized, low-frequency payments where decentralization's inefficiencies are acceptable. It excels in *niche* use cases, cross-border remittances or privacy-focused transfers (money laundering, hello) but fails as a universal financial rail. Without solving scalability or reintroducing trust mechanisms, blockchain remains impractical for mainstream, high-volume finance. The future lies in hybrid systems, not dogmatic decentralization.

Stablecoins represent the crypto industry's most audacious gambit: transforming intangible blockchain tokens into real-world liquidity. Before their rise, exiting large crypto positions required navigating opaque OTC desks or questionable exchanges. Now, stablecoins offer a seamless off-ramp, a way to monetize crypto currencies nearly USD 4 trillion valuation without triggering tax events or price slippage.

This liquidity bridge has supercharged crypto's speculative frenzy. Traders collateralize Bitcoin to borrow stablecoins, then leverage those stablecoins to buy more Bitcoin, a recursive loop detached from intrinsic value, if there is any. Wider use and higher trading volume also helps push up values of Ethereum, brick and mortar to build infrastructure. The result is a system where crypto wealth exists primarily as a self-referential bet on its own adoption, with stablecoins serving as the escape hatch.

The political dimension is equally fraught. The Trump administration's embrace of crypto, including Trump's own NFT ventures and pro-mining policies, has given the industry unprecedented legitimacy. However, a Democratic administration might reverse this stance, particularly given stablecoins' role in circumventing financial controls. The coming election could prove existential for crypto's regulatory landscape.

Proponents argue that USD-backed stablecoins reinforce dollar hegemony by spreading greenback usage offshore. But this view ignores how stablecoins could accelerate de-dollarization. Unlike physical dollars, which require banking infrastructure, stablecoins can be minted against any fiat currency, a feature that China and other rivals are keen to act and dilute the power dollar monopoly in fiat currency world.

The numbers are telling: RMB's share of global trade finance has surged from under 2% in 2020 to over 7% today, rivaling the euro. As China dominates global trade, a digital RMB stablecoin, likely launched via Hong Kong's 2026 regulatory framework, could leverage this network effect to bypass dollar clearing entirely. Imagine a Brazilian importer paying a Chinese supplier in RMB-backed stablecoins, settled instantly on-chain without touching SWIFT or correspondent banking. The implications for

dollar dominance are profound. Right here sits one market implication for dollar weaker and RMB stronger in the process.

The crypto bubble's most dangerous feature is its entanglement with traditional finance. Bitcoin's robust correlation to Nasdaq since 2020 reveals how deeply crypto fortunes are tied to risk appetite in tech stocks. NVIDIA's GPU sales to miners, Coinbase's custody fees, and Tether's commercial paper holdings all intertwine crypto with mainstream markets.

This linkage creates a perilous feedback loop. A crypto crash would vaporize collateral for leveraged positions, forcing liquidations that ripple into equity markets. Stablecoin issuers, which park reserves in short-term Treasuries, could trigger bond market turbulence if forced to dump holdings during a panic. Even AI stocks aren't immune; many trades at valuations premised on crypto-driven demand for data centers and chips.

The crypto payment-sector IPOs now flooding markets are particularly vulnerable. This is a dangerous sign. Crypto world is trying to cash out in traditional finance using the frenzy. Their margins rely on regulatory arbitrage that will vanish as banks compete, and government regulates.

To summarize, the crypto experiment has birthed two contradictory truths: it is simultaneously a revolutionary proof-of-concept for decentralized finance and a speculative casino propped up by regulatory gaps and yield-chasing capital. Stablecoins, far from being crypto's salvation, are potentially its most dangerous innovation, a mechanism for laundering volatility out of digital assets and into the real economy.

The coming years will test whether this ecosystem can survive its own contradictions. Hong Kong's RMB stablecoin push may spark a geopolitical currency war, while US political shifts could deflate crypto's regulatory protections. Most critically, the \$4 trillion question remains: Can crypto transition from a vehicle for gambling to a system with genuine utility? That is what the crypto world is working toward, pinning their hope on RWAs (Real World Assets) and creating a parallel playhouse to traditional banking.

With so many at work and so much at stake, the effort will likely yield some success, as we see more RWA financing coming online. But I am a skeptic for the philosophical reasons mentioned above.

There is one more point in consensus beliefs. Though the trust in Bitcoin seems to be invincible in certain sets of people, the region barely crosses its 15-year mark, unlike gold enduring centuries of tests. What if next generation rebels against the value system to buy from the current generation on a digital asset with little intrinsic value. On generation break for value destruction and creation, think about recent transit from stamp to Air Jordan (Labubu now?) collection.

Investors beware; there are no safe havens from speculative excess.

Risk: Three Concerns for September

In September, global financial markets face three distinct, but potentially interconnected risks threaten to disrupt what has been a remarkably resilient year for risk assets. From Beijing to Washington to Tokyo, policymakers and investors alike are grappling with events that could trigger significant market repricing, not because of traditional economic fundamentals, but due to political and psychological factors that often prove far more volatile than earnings reports or GDP prints.

First, China's victory parade may turn out to be a classic "buy the rumor, sell the news" setup. The upcoming September 3rd event in Beijing, commemorating the 80th anniversary of China's victory in the anti-fascist war against Japanese aggression, has become an unlikely focal point for market anxiety. Historically, such events have served as both patriotic showcases and policy signaling platforms, with the government typically engineering favorable market conditions in the lead-up. This year appears no different: the CSI 300 has rallied 13% since end of June, supported by a noticeable relaxation of margin requirements and strong retail sentiment, both subject to quick turns. Some may use the event as an excuse to sell.

Market psychology surrounding these events follows a predictable pattern, the "national team" prop up markets beforehand, creating an artificial sense of buoyancy that retail traders invariably chase. Yet once the political objective is achieved, support tends to evaporate. Margin debt has surged to near-2015 levels, short-term technical indicators are flashing overbought signals across Chinese benchmarks.

The parade's timing exacerbates these risks. September traditionally marks the beginning of China's "political season," with the Party's 4th plenum in October with heightened uncertainty on personnels and central work conference in December to roll out 15th five-year plan. This creates a natural incentive for policymakers to conserve both fiscal and regulatory ammunition for more politically sensitive periods later in the year. Combined with lingering concerns about property sector stability and lackluster July economic data to continue in August, the stage appears set for Chinese equities give back some of their summer gains just as global investors return from summer holidays.

Across the Pacific, Wall Street is bracing for its own seasonal reckoning. September has historically been the worst month for US equities, with the S&P 500 return averaging -4% / -2% in the last 5/10 years, a phenomenon so persistent that traders have dubbed it the "September Effect." While skeptics dismiss this as statistical noise, a few factors stare right back.

The first wildcard is positioning. Hedge fund net exposure currently sits near 18-month highs, while systematic strategies like CTAs and risk parity funds have ramped up equity allocations to levels last seen before the 2022 bear market. This crowded trade leaves markets vulnerable to any catalyst that might trigger synchronized de-risking. Meanwhile, retail investors, whose options activity often serves as a contrarian indicator, have piled into short-dated call options at a pace not seen since January

2022, precisely before last year's 20% correction. Last, VIX selling position also tops the chart.

Perhaps more ominously, the market's leadership has narrowed dramatically, with the "Magnificent Seven" tech stocks now accounting for over 90% of the S&P 500's year-to-date gains. Such extreme concentration has reliably preceded past market breakdowns, as occurred in 2000 and 2007.

Adding fuel to this combustible mix is an unprecedented political shockwave rippling through the Federal Reserve. President Trump's abrupt dismissal of Governor Lisa Cook has introduced a dangerous new variable into monetary policy calculus and calls into the question of central bank independence. Markets initially shrugged off the news as political theater, but beneath the surface, the implications could prove far more destabilizing than currently appreciated.

Cook's removal threatens to politicize monetary policy at precisely the wrong moment. With inflation still above target and the Fed's credibility hanging in the balance, Powell now faces governing board dynamics where every decision risks being viewed through an overtly political lens. This comes as the Fed attempts to navigate its trickiest policy transition since Volcker, shifting from rapid hikes to a "higher for longer" stance without triggering a recession. Historically, such transitions have required near-unanimous consensus among policymakers to maintain market confidence. The current fight picked by Trump on Fed reminds investors the fight between Reagan and Fed in 80s. Volcker quit in June 1987; the market crashed in October, which was saved by Greenspan put. The history might not repeat, but we heard the rhyming loud and clear.

The timing couldn't be worse. With September cut nearly priced in, Cook's firing might entrench Powell in his Polcker Rule decision, i.e. he may decide not to cut, assuming September payroll is in line and CPI rises as expected, just for the sake of Volcker part of Fed independence. The VIX term structure reflects early signs of stress, with October and November contracts trading at unusual premiums to near-dated ones—a pattern last seen before the 2018 "Volmageddon" selloff. A lack of cuts in September could prompt this action.

These three risks might appear unrelated at first glance. Yet they share a common thread: each represents a potential catalyst that could transform simmering market vulnerabilities into full-blown corrections. China's retail-driven rally looks unstable, US markets are priced for perfection amid deteriorating fundamentals, and the Fed's ability to backstop turbulence may be compromised just as seasonality kicks in.

For us, the critical question isn't whether these risks will materialize, it's how they might interact if they do. History suggests that when political, seasonal, and structural risks converge, markets tend to reprice faster and more violently than fundamentals alone would justify.

Cheap VIX seems to offer the best hedge.

Asset: China's Anti-Involution at Work

The US stock rally extended into mid-August, brushing aside concerns on August 12th deadline for tariff kick-ins. US tech giants led the charge, with expanding capital expenditures and strong earnings reports pushing valuations higher and reinforcing bullish sentiment toward AI-related sectors. This optimism coincided with China's A-share market, where hardware-focused AI plays drove significant outperformance in the ChiNext Index. The anticipated DeepSeek upgrade cycle also fueled gains across AI application stocks, while positive sentiment rippled into the semiconductor sector, lifting previously laggard STAR index.

The Politburo meeting emphasized anti-involution and anti-deflationary measures, helping the Shanghai Composite reclaim post-National Day highs. Hang Seng Index initially tracked A-shares higher but faltered in late July as dollar strength resurfaced, tightening liquidity conditions despite robust southbound inflows.

Looking ahead, the bull run may take a breath with major macro catalysts now behind us. While external capital inflows should provide downside support, the upcoming event may come as a "sell on the news" as discussed in the risk section.

The rates market endured a challenging month, with the 1-year and 10-year CGB yields rising 4.05 bps and 5.75 bps respectively, resulting in a bear steepening of the curve. Three primary factors drove the selloff: anti-involution and anti-deflation policies in the Politburo meeting, commodity price surges, raising fear of PPI turning positive soon, and equity market strength diverting funds from fixed income.

Notably, bond funds inflows turned to outflows, prompting duration reduction among top performers. Rural commercial banks emerged as unlikely buyers of duration during the selloff. The market ultimately stabilized by mid-to-late August.

Looking forward, the insurance sector's announced cuts to guaranteed policy rates should drive premium growth in August, while maturing large-denomination CDs create hope for non-bank demand. We see these flow driven buying as an opportunity to add short to super long-term bonds since they are not to be repeated for the rest of the year.

In commodity space, steel markets exhibited unusual seasonal strength amid macro-driven sentiment. While demand improved sequentially from June, year-on-year comparisons remained negative. The sector displayed clear bifurcation: construction steel suffered from extreme weather and liquidity constraints, while manufacturing-focused ones demonstrated resilience, supported by export orders.

Rebar faces mounting supply pressure as electric arc furnace producers return to profitability and blast oxygen furnace operators maintain high operating rates. Though inventories remain lean, September stockpile risks are rising as production turns positive year-on-year. Hot rolled coil supply hit record highs, with near-term demand supported by mills' order

backlogs. However, downstream pressures are mounting, leading to negative processing margins with auto and appliance sectors showing signs of fatigue.

Iron ore maintains a delicate balance, with port inventories stable despite strong blast furnace utilization. The market lacks clear directional catalysts. We expect weaker demand-supply balance ahead and remain negative on the commodity.

Crude oil prices staged a late-month rally on geopolitical tensions, closing above USD 70 / bbl after Trump threatened secondary sanctions on Russian crude. Fundamental drivers remain mixed as the market faces a "strong spot, weak forward" dynamic. Weather wise, the chance of another La Nina is increasing. Though still early, it may lead to cold winter in the US and potentially create opportunities for buy-on-dip in Jan/Feb natural gas, alone or against TTF with which HH will converge as Europeans buy more US gas.

In currency, the CNY starts to strengthen following typical seasonal pattern. The PBOC is more willing to guide USD/CNY lower through its daily fixings, partially attributing to the confidence in winning the trade war fight with the US. Seasonally, China's trade surplus widens in the second half, with exporters converting FX receipts ahead of dividend payments and year-end obligations. The PBOC's fixing creates urgency in corporates feared a repeat of last year.

Technically, USD/CNY has broken below its 200-day moving average, a level that has capped declines in recent months. Momentum suggests further near-term downside, though the pace may slow as state banks reportedly emerge to smooth volatility. We favor long CNH against THB, whose central bank may continue cutting rates to support the economy.

Capital: China's Liquidity Surge

China's financial markets are currently caught in the grip of a powerful liquidity-driven rally, one that is being shaped not by the usual suspects of foreign capital inflows or government stimulus announcements, but rather by a confluence of domestic retail enthusiasm, institutional reallocation, and an unexpected surge in broad money supply. July's data revealed a dramatic shift in where money is moving, how it is being deployed, and why the current equity uptrend may have further to run, even if the road ahead isn't entirely free of potholes. At the heart of this dynamic is a simple but profound truth: Chinese households and institutions are finally putting idle cash to work.

Start with the most visible sign of renewed retail engagement: the surge in new stock accounts. In July alone, 1.96 million new A-share accounts were opened, marking a 19% increase from the previous month. While this figure remains shy of the frenzied highs seen during 2020 and last September, it is nonetheless a meaningful acceleration, particularly when viewed in the context of the broader market rally that gained traction throughout August.

What's more, this retail revival is not being confined to speculative corners of the market. While initial flows did indeed gravitate toward high-growth sectors such as technology and biotech, areas that have historically attracted retail momentum, it has since broadened out to more index-heavy names with ETF AUM rising another RMB 1 trillion in merely four months to 5 trillion. A wider pool of investors begins to view the equity market as a viable destination for their savings.

Compounding this retail resurgence is the equally noteworthy pickup in leveraged betting, as evidenced by the fact that margin debt has now climbed to a decade-high of RMB 2.13 trillion. This level of margin utilization is approaching the extremes seen during the 2015 market bubble, a comparison that inevitably raises red flags among cautious observers. Yet, unlike the 2015 episode, where margin debt was accompanied by widespread speculative fervor and a lack of fundamental underpinnings, the current environment appears to be supported by a more robust foundation of liquidity and a broader reallocation of household savings. Also, the monetary base measured in M2 has more than doubled, making the margin loan level less worrisome.

The key difference lies in the scale of the cash influx: July witnessed an extraordinary RMB 2.5 trillion shift in deposits, as households moved money out of traditional savings vehicles in pursuit of higher returns. The sheer magnitude of this cash movement has effectively overwhelmed the lingering skepticism of foreign investors, who continue to exit Chinese equities at a steady clip. Passive money, however, is being dragged along by index rebalancing mechanisms, ensuring that the tailwind of liquidity persists even in the absence of strong foreign conviction.

The picture on the institutional side looks equally compelling. Chinese insurers, long known for their conservative asset allocation strategies, are quietly but decisively increasing their exposure to equities, lifting their stock allocations to a three year high 8.81% of total portfolios. Property and casualty insurers have followed suit, pushing their equity weightings to 8.33%. This strategic shift is being driven by a combination of factors, including the low bond yields and subtle policy encouragements steering more capital toward equities.

The implications of this institutional reallocation are significant, as insurers represent a class of investors with long-term horizons and substantial capital bases, meaning their increased equity exposure is unlikely to be a short-term phenomenon. Instead, it points to a more structural rotation of institutional assets into the equity market, which could provide a stabilizing influence on market dynamics as the politically correct “patient capital (耐心资本)” over the medium term.

Adding to the liquidity-driven momentum is the record-breaking surge in southbound flows, which reached an astonishing RMB 135.7 billion in July. These flows, which represent mainland Chinese investor purchases of Hong Kong-listed stocks, have been driven in large part by the allure of technology stocks, which have drawn listings away from traditional

dividend plays. Single-day flows spiked to as high as RMB 35.9 billion, underscoring the intensity of investor interest in this segment of the market. The southbound rush is a critical component of the broader liquidity picture, as it represents a significant channel through which domestic savings are being funneled into equities.

This trend has been notable for its potential to compress valuation disparities between A- and H-shares, particularly in the technology sector, where Hong Kong-listed stocks have historically traded at a steep discount to their mainland counterparts. The narrowing of the AH premium, which currently stands at 125 (A is 125% of H) from March's 155, suggests that this dynamic is already taking hold with room for further convergence before the arbitrage opportunity is fully exhausted.

The macro-level backdrop to these flows is equally instructive. The surprise uptick in M2 growth, which came in at 8.8% for July compared to expectations of 8.3%, underscores the continued abundance of liquidity in the Chinese financial system. This elevated level of broad money supply is not merely a statistical anomaly; it is the result of a deliberate policy stance that has prioritized liquidity provision as a means of supporting economic activity in the face of external headwinds.

Similarly, the stronger-than-expected M1 growth of 5.6%, versus expectations of 5.2%, points to continued increase of money available for immediate deployment in both household and corporate sectors, a trend we discussed in previous months. Together, these metrics paint a picture of a financial system that is awash in liquidity, with money moving from the sidelines into productive uses at an accelerating pace.

The implications of this liquidity surge are far-reaching. For one, it suggests that the current equity market rally is not merely a short-term phenomenon driven by speculative excess, but rather a more sustainable rotation of capital into equities, supported by a confluence of retail enthusiasm, institutional reallocation, and macro-level liquidity abundance.

However, this is not to say that the path ahead is without risks. Two key risks merit attention: redemption pressure from 2021 fund investors as NAV nears breakeven, which could temporarily weigh on market momentum, especially during volatile periods. Second, the narrowing AH premium, while still providing room for further convergence, could begin to lose its appeal as a driver of southbound flows. CSRC's rule excluding H shares when counting insurer's equity holding may also lead to some sell-off pressure in Hong Kong.

For medium outlook, however, the dominant narrative remains one of liquidity-driven upside. The combination of retail resurgence, institutional reallocation, and macro-level liquidity abundance has created a virtuous cycle of capital flows that is supporting market momentum. The key takeaway is that China's financial markets are undergoing a significant transformation, driven not by external factors but by the internal dynamics of liquidity migration and risk appetite expansion.

Economy: A Tale of Three Economies

The global economic landscape in July presented a study in contrasts, with China, the US, and Japan each navigating distinct challenges and opportunities. Beneath the surface of headline growth figures, these economies are experiencing micro-level fractures that reveal deeper structural shifts, some cyclical, others potentially secular. The data tells a story of divergence, where traditional economic indicators no longer move in lockstep, creating what Chinese often describe as an "ice and fire dichotomy (冰火两重天)."

The US economy continues to exhibit what can only be described as a split personality. On one side, the labor market shows unmistakable signs of softening. July's jobs report disappointed across multiple dimensions with nonfarm payrolls at their slowest pace this year, wage growth stagnated, and retail sales unexpectedly contracted for the third consecutive month. The University of Michigan consumer confidence has deteriorated sharply, reflecting growing anxiety over inflation's stubborn persistence and the high financing costs. Traditional economic pillars including housing, autos, and consumer discretionary spending are clearly feeling the pinch of tighter financial conditions.

Yet juxtaposed against this weakness is an extraordinary boom in AI and related technologies. Nasdaq's relentless rally, now in its sixteenth month, shows no signs of fatigue as AI-enabling companies continue to post blistering revenue growth.

This divergence has created a peculiar dynamic where Wall Street celebrates while Main Street struggles, a modern iteration of the "two-track economy" phenomenon that has periodically emerged throughout US economic history. The critical question now is whether the AI boom can generate enough spillover effects to offset weakness elsewhere, or when an isolated bright spot fails to support the hefty valuation.

While US faces the split between AI and retail, China's July economic data painted a similarly bifurcated picture, though with very different contours. On the external front, trade figures surprised strongly to the upside with exports growing 7.2% YoY, and imports expanding by a robust 4.1%. Both figures comfortably exceeded consensus estimates and together spit another month of trade surplus around USD 100 billion. This performance was particularly notable given the global growth slowdown, suggesting Chinese exporters are gaining market share even as demand softens. The temporary truce in the US-China tariff war will keep the tailwinds blowing and support growth.

Domestically, however, the situation remains concerning. Retail sales growth slowed to just 3.7% YoY, well below both tepid 4.6% expectations and June's already low 4.8% reading. Industrial production growth decelerated marginally to 6.3% from 6.4%, while YTD property investment growth slipped to -12.0% from -11.2% the month before, suggesting a severe deterioration in July. The new home prices fell in 49 of 70 major cities, and developer financing conditions remain tight despite

incremental policy easing. This domestic weakness stands in stark contrast to the export sector's vigor, creating a peculiar dynamic where China's economic health is increasingly dependent on external demand even as policymakers emphasize the need for "dual circulation (双循环)."

The divergence between China's external and internal economic engines poses significant policy challenges. On one hand, strong trade performance provides a crucial buffer against domestic softness, helping maintain overall GDP growth above 5%. On the other, over-reliance on exports makes the economy vulnerable to potential protectionist measures later this year, as trade war deadline approaches. Meanwhile, the persistent weakness in household consumption suggests that Beijing will continue policies to rebalance growth toward domestic demand.

Japan's economy presents perhaps the most intriguing case of the three, with traditional indicators sending conflicting signals about its underlying health. The economic surprise index has hovered near 30, at the upper end of its three-year range. The manufacturing PMI recovered to 49.9 from 48.9, while services PMI declined slightly to 52.7. Together they still push the composite to 51.9 from 51.6, reflecting broad-based strength across sectors. Corporate earnings have been robust, with export-oriented firms benefiting from yen weakness and domestic companies seeing improved pricing power after decades of deflationary pressures.

Yet Japan's labor market tells a different story. The jobs-to-applicants ratio unexpectedly tumbled to 1.22 in July, its lowest level since 2021. This decline, which came despite solid GDP growth, mirrors similar disconnects seen in US data and raises questions about the reliability of traditional labor market indicators in post-pandemic economies.

What makes Japan's situation particularly noteworthy is how it encapsulates the global economy's broader uncertainties. On paper, Japan should be thriving with inflation finally positive after decades of deflation, corporate profits strong, and the weak yen providing a powerful tailwind for exporters. Yet beneath these encouraging signs lurk persistent concerns about demographic headwinds, productivity stagnation, and the sustainability of wage growth needed to sustain inflationary momentum.

Wider labor participation may offer help in consolidating the data and offsetting demographic worries. Total participation rate has recovered from 2013's low of 58.5% to 64.2% and is still rising. The most notable among the labor force is the female participation rate, rising from a stagnate 48% in 2002-2012 ten-year low average to today's high 56.9%. The number still lags Korea's 57.3% and much behind China's 83%, thus offers hope for further labor participation to support growth.

Beneath these three distinct economic narratives run several unifying themes. First, traditional economic models are struggling to explain current dynamics, as long-standing relationships between labor markets, consumption, and growth appear to be breaking down. Second, technology is creating new growth vectors that don't always align with

broader economic cycles, AI in the US, advanced manufacturing products dominating the world in China, and cheap currency high quality experience attracting more tourists and creating service jobs in Japan. Third, all three economies are grappling with the challenges of policy normalization after years of extraordinary stimulus, though their approaches differ markedly.

For us, navigating this new landscape will require moving beyond traditional frameworks and developing fresh lenses for understanding economies that increasingly resemble patchworks of strength and weakness rather than uniform wholes. One thing seems certain: the old rules no longer apply, we need new playbooks, very different ones.

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End notes