

WORLD ECONOMIC OUTLOOK

WORLD FINANCIAL MARKETS - WORLD FINANCIAL STATE - TAIWAN - CHINA - WAR IN UKRAINE

HUGHES ECONOMICS (HE) – 13th March 2023

The current review below calculates probabilities for Financial Markets outcomes, the situation over Taiwan, the possibility of another depression, China’s direction in world affairs and the war in Ukraine. All papers as below are available on this website as are various spreadsheets in **xlsx** format. All calculations below employed the **WE Omar.xlsx** spreadsheet using **LoHiProbs.xlsx** methodology.

Probability calculations below for the scenarios outlined are explained in **Structuring Probability Assessments** available at <https://doi.org/10.17265/1537-1506/2020.05.003>. Also **Thinking Probabilistically** available at <https://doi.org/10.17265/1537-1506/2021.05.002>, **Thinking Probabilistically Revisited** available at <https://doi.org/10.17265/1537-1506/2022.01.001>, **A New Approach to Probability Assessment** available at <https://doi.org/10.17265/1537-1506/2022.01.003> and **Probability Assessment** available at <https://doi.org/10.17265/2328-2185/2022.05.006>. A summary article **Assessing Probabilities With Minimal Calculations** can be downloaded from this website.

WORLD FINANCIAL MARKETS (WFM)

As stated previously, three possible scenarios are proposed for the next 6 months as listed below in order of increasing likelihood:

- **TINA:** There is no alternative, and the Dow rises significantly to 40,000+.
- **SQ:** Status Quo, no major moves for the Dow in the range 30,000 – 35,000. Current Dow is around 32,000.
- **BB:** Bubble bursts and Dow corrects to significantly below 30,000 or a 10%+ correction from current levels.

PROBABILITIES ON WORLD FINANCIAL MARKETS FOR THE NEXT 6 MONTHS

Scenarios		Pairwise Range		Probabilities					More Likely Value
Events	Ratios	Low	High	Low End	High End	Average	%	Previous	
TINA	Base = 1	1.00	1.00	0.020	0.014	0.017	2	3	Base = 1
SQ	SQ/TINA	10.00	12.00	0.196	0.164	0.180	18	28	10.59
BB	BB/SQ	4.00	5.00	0.784	0.822	0.803	80	69	4.46
				1.000	1.000	1.000	100	100	

The above probabilities have been recalibrated following the reappraisal of the **WFS** below.

WORLD FINANCIAL STATE (WFS)

Scenarios in order of increasing likelihood are as follows:

- **MB** or Mild Boom: Revamping of world infrastructure in light of Ukraine sees markets rise for 10%+ gains.
- **D** or Depression: High inflation and continued COVID pressures, policy mistakes and global financial collapse.
- **SQ** or Status Quo: Stalemate in Ukraine, inflation cools, labour markets remain healthy.
- **MR** or Mild Recession: World activity falls, with problems from COVID, Ukraine, ESG factors & supply chain realignments.

PROBABILITIES ON THE WORLD FINANCIAL STATE FOR THE NEXT 6 MONTHS

Scenarios		Pairwise Range		Probabilities					More Likely Value
Events	Ratios	Low	High	Low End	High End	Average	%	Previous	
MB	Base = 1	1.00	1.00	0.006	0.003	0.005	1	1	Base = 1
D	D/MB	10.00	12.00	0.062	0.040	0.051	5	6	10.20
SQ	SQ/D	3.00	4.00	0.186	0.159	0.173	17	21	3.39
MR	MR/SQ	4.00	5.00	0.745	0.797	0.771	77	72	4.46
				0.999	0.999	1.000	100	100	

Mohamed El-Erian recently gave higher inflation outcomes a 75% likelihood. **HE** has formed the judgment that this is indeed a likely outcome. ESG concerns and a realignment of more secure if more expensive supply chains mean 2% inflation (the Fed target) over the next 2 – 3 years has a low chance of prevailing unless drastic action takes place now. The Fed may decide that only higher interest rates for longer will secure the 2% rate and, if so, this does not bode well for markets. Only other unlikely events, as in

Russia failing badly in Ukraine, could raise the chance of the world avoiding some form of recession. Accordingly, the probability of **MR** increases as above.

TAIWAN

The scenarios for developments involving Taiwan from least to most likely are as follows:

- **TINO**: Taiwan invasion by mainland China with no aid from any country to help repel the invaders.
- **TIUS**: Taiwan invasion by mainland China and the US assists Taiwan in its defense, possibly with other allies.
- **NOTI**: No invasion of Taiwan but Chinese harassment of Taiwan continues.

PROBABILITIES ON TAIWAN DEVELOPMENTS OVER THE NEAR FUTURE

Scenarios		Pairwise Range		Probabilities					More Likely
Events	Ratios	Low	High	Low End	High End	Average	%	Previous	Value
TINO	Base = 1	1.00	1.00	0.038	0.020	0.029	3	5	Base = 1
TIUS	TIUS/TINO	5.00	7.00	0.192	0.140	0.166	17	21	5.72
NOTI	NOTI/TIUS	4.00	6.00	0.769	0.840	0.805	80	74	4.85
				0.999	1.000	1.000	100	100	

There are no changes from last month.

CHINA'S FUTURE DIRECTION

Outcomes in increasing order of likelihood are as follows:

- **RDA**: Regionally decentralized authoritarianism – initially orchestrated by Deng Xiaoping leading to China's rapid rise.
- **RD?**: Some hybrid model incorporating aspects of RDA and avoiding the worst excesses of RDT which follows.
- **RDT**: Regionally decentralized totalitarianism – a top down economic system with no freedom in regional decision-making.

Under RDA, regions were allowed to make their own economic decisions and this competition between them advanced the Chinese economy significantly, but with some Western market characteristics. It would seem that the CPC will tolerate economic underperformance with **RDT** for some years before deciding a change in tack is required and **RDT's** probability increases again this month.

PROBABILITIES ON POSSIBLE CHINESE DEVELOPMENTS

Scenarios		Pairwise Range		Probabilities					More Likely
Events	Ratios	Low	High	Low End	High End	Average	%	Previous	Value
RDA	Base = 1	1.00	1.00	0.040	0.027	0.034	3	12	Base = 1
RD?	RD?/RDA	3.00	4.00	0.120	0.108	0.114	12	12	3.35
RDT	RDT/RD?	7.00	8.00	0.840	0.865	0.852	85	76	7.47
				1.000	1.000	1.000	100		

THE WAR IN UKRAINE

The scenarios following are in line with *The Economist's* appraisals in a recent publication. In order of likelihood these are:

- **CRT**: A ceasefire is negotiated but on terms dictated by Russia.
- **CUT**: As for **CRT** but with Ukraine dictating the terms.
- **STM**: A stalemate cements itself with battlelines little changed from those currently operational.

PROBABILITIES ON POSSIBLE OUTCOMES TO THE WAR IN UKRAINE

Scenarios		Pairwise Range		Probabilities					More Likely
Events	Ratios	Low	High	Low End	High End	Average	%	Previous	Value
CRT	Base = 1	1.00	1.00	0.063	0.040	0.051	5	7	Base = 1
CUT	CUT/CRT	3.00	4.00	0.188	0.160	0.174	17	17	3.41
STM	STM/CUT	4.00	5.00	0.750	0.800	0.775	78	76	4.45
				1.001	1.000	1.000	100	100	

HE has formed the judgment that the West led by the US is determined that Putin will not win. Although it may take time, only bad news lies ahead for Russia.