

WORLD ECONOMIC OUTLOOK – FINANCIAL MARKETS & THE BIG PICTURE

HUGHES ECONOMICS – JANUARY 2021

The current review below updates probabilities for Financial Markets outcomes and the World Economic Order focusing on the emergence of China in coming years as a rival to current USA hegemony.

WORLD FINANCIAL MARKETS

Three possible scenarios are proposed for the next 6 months:

1. TINA: There is no alternative and the Dow rises significantly to 34,000 – 40,000 (prior probability 19%).
2. BB: Bubble bursts and Dow corrects to 25,000 – 30,000 or 10%+ correction (38%).
3. SQ: Status Quo with no major moves for the Dow in the range of 30,000 – 34,000 (43%).

Prior probabilities were derived in a previous WEO briefing (see hugheseconomics.com). Democrats with Biden swept the elections and now control the Presidency, Senate and the House. A second impeachment of Trump is a possibility. This “news” is reflected in the following “more likely” or “more consistent” judgments in the table below. The least consistent scenario with current developments is TINA at the base level 1.0.

CONSISTENCY OF “NEWS” WITH POSSIBLE SCENARIOS FOR WORLD FINANCIAL MARKETS

Scenario	Pairwise Judgment	Compound Likelihood	Probability	Percent Probability
TINA	1.00	1.00	$1.00/6.405 = 0.156$	16
BB	2.30	$1.00 \times 2.30 = 2.30$	$2.30 / 6.405 = 0.359$	36
SQ	1.35	$2.30 \times 1.35 = 3.105$	$3.105/6.405 = 0.485$	48
		6.405	1.000	100

BB is seen as more than twice as likely as TINA with SQ significantly “more likely” than BB at this point in mid-January. Updated probabilities for the possible scenarios are shown below.

POSTERIOR PROBABILITIES FOR POSSIBLE SCENARIOS ON WORLD FINANCIAL MARKETS

Scenario	Prior	Likelihood	Joint	Posterior	Percent
TINA	0.188679	0.156128	0.029458	0.078484	8
BB	0.377358	0.359094	0.135507	0.361024	36
SQ	0.433962	0.484778	0.210375	0.560492	56
	0.999999	1.000000	0.375340	1.000000	100

Tax increases to pay for the Covid-19 outbreaks are now more likely in the US. And Democratic over-reach may stall necessary fiscal stimuli there. Brexit so far is not a big issue for the world economy. The BB scenario is still a sizeable 36% chance. Covid-19 continues to cause problems for many countries, but vaccination rollouts could minimize any resulting fallout from the virus going forward.

WORLD ECONOMIC ORDER

China's economic recovery seems set to continue. But Biden's canniness should preserve US hegemony for the foreseeable future. Possible scenarios are as follows:

1. China: China overtakes the US as world leader (prior probability 10%).
2. Cold War 2: The US and China compete for world leadership with major ramifications for some countries (30%).
3. USA: The US continues as world leader with China relegated to second place for the foreseeable future (60%).

Questions have arisen as to the Chinese Communist Party's (CCP) intentions with regard to major corporate leaders such as Jack Ma and the CCP's future involvement with world-wide business development. Currently, the CCP's policies may inhibit Chinese world leadership in major sectors such as finance. A clear change in direction of CCP policy will be needed before China can seriously challenge US world leadership. And US institutions and corporations are fully aware of the challenge China now poses. A "news" update of this current situation follows.

CONSISTENCY OF "NEWS" WITH POSSIBLE SCENARIOS FOR THE WORLD ECONOMIC ORDER

Scenario	Pairwise Judgment	Compound Likelihood	Probability	Percent Probability
China	1.00	1.00	$1.00/8.5 = 0.118$	12
Cold War 2	2.50	$1.00 \times 2.50 = 2.50$	$2.50/8.5 = 0.294$	29
USA	2.00	$2.50 \times 2.00 = 5.00$	$5.00/8.5 = 0.588$	59
		8.50	1.000	100

Note that Cold War 2 is not seen as "likely", but it is between two and three times "more likely" than a Chinese hegemony under the current outlook. Continuing USA world leadership is seen as twice as likely as Cold War 2. The higher the pairwise judgments are, the lower the probabilities for preceding events in the order. Updated probabilities for the new world order are calculated below.

POSTERIOR PROBABILITIES FOR POSSIBLE SCENARIOS ON THE WORLD ECONOMIC ORDER

Scenario	Prior	Likelihood	Joint	Posterior	Percent
China	0.10	0.117647	0.011765	0.025974	3
Cold War 2	0.30	0.294118	0.088235	0.194805	19
USA	0.60	0.588235	0.352941	0.779221	78
	1.00	1.000000	0.452941	1.000000	100

A continuation of US hegemony is seen as almost an 80% chance (previously 60%) to continue at this point in January 2021. China has almost a negligible chance of assuming world leadership in the near future. Hostile relations between the US and China are seen to be a 4:1 possibility with major ramifications for Taiwan, North Korea, Central Asia, the South China Seas and other countries. Of course, different primary judgments for the pairwise assessments would lead to different probabilities. Future developments will be incorporated in the above judgments as they manifest themselves.