

WORLD ECONOMIC OUTLOOK – FINANCIAL MARKETS & WORLD ECONOMIC ORDER

HUGHES ECONOMICS (HE) – February 2022

The current review below restates probabilities for Financial Markets outcomes, the World Economic Order focusing on the US versus China and the possibility of another depression. As another demonstration of the methodology favoured here, the origins of the COVID-19 virus are examined in the paper on this website *Thinking Probabilistically VI*.

WORLD FINANCIAL MARKETS

As stated previously, three possible scenarios are proposed for the next 6 months as listed below in order of increasing likelihood. The Status Quo as defined below is seen as most likely to continue.

1. **BB**: Bubble bursts and Dow corrects to 30,000- or a 10%+ correction.
2. **TINA**: There is no alternative, and the Dow rises significantly to 40,000+.
3. **SQ**: Status Quo with no major moves for the Dow around 35,000 – as of 31/1/2022, the Dow is at 35,132.

Probability calculations below for the above scenarios 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> and *Thinking Probabilistically Revisited* available at <https://doi.org/10.17265/1537-1506/2022.01.001>. All papers are available on this website.

PROBABILITIES ON FINANCIAL MARKETS FOR UP TO THE NEXT 6 MONTHS

Scenario	Pairwise Judgment	Compound Likelihood	Probabilities	Percent Probabilities	
				Current	Previous
BB	1.00	1.00	$1.00/5.5 = 0.1818$	18	14
TINA	1.00	$1.00 \times 1.00 = 1.00$	$1.00/5.5 = 0.1818$	18	22
SQ	3.50	$1.00 \times 3.50 = 3.50$	$3.50/5.5 = 0.6364$	64	64
TOTALS		5.50	1.0000	100	100

Jeremy Grantham's view that the bubble is bursting for US markets has received wide coverage recently. HE's view is that **TINA** is equally likely with **BB** and that **SQ** is between 3 and 4 times more likely than either **BB** or **TINA** (a 64% chance to continue). The logic of **TINA** is that even though conventional metrics suggest stocks are over-valued, currently it is a unique **TINA** situation and stocks could go higher still. Of course, geopolitical developments in Ukraine, Taiwan, Iran or elsewhere would change the above probabilities drastically.

WORLD ECONOMIC ORDER

To restate all the possibilities, we have, in increasing order of likelihood:

1. **China**: China overtakes the US as world leader or Chinese hegemony.
2. **Cold War 2**: The US and China compete vigorously for world leadership with major ramifications for some countries.
3. **USA**: The US continues as world leader with China relegated to second place for the proximate future.

These scenarios will play out over the next 10 years. Current probabilities are calculated below:

PROBABILITIES ON THE WORLD ECONOMIC ORDER EVOLVING OVER THE NEXT DECADE

Scenario	Pairwise #	Compound Likelihood	Probabilities	Percent Probabilities	
				Current	Previous
China	1.00	1.00	$1/31 = 0.032$	3	2
Cold War 2	10.00	$1.0 \times 10.00 = 10.00$	$10/31 = 0.323$	32	16
USA	2.00	$10.0 \times 2.00 = 20.00$	$20/31 = 0.645$	65	82
TOTALS		31.00	1.000	100	100

No change is proposed in the probabilities for possible World Economic Orders. In the November 2021 calculations, **Cold War 2** gained in likelihood at the expense of USA hegemony, but the **USA** scenario is still seen as a very likely 65% chance in February 2022.

WORLD FINANCIAL STATE

Scenarios in order of increasing likelihood are as follows:

D or Depression: High inflation and continued COVID-19 pressures, policy mistakes and global financial collapse.

MB or Mild Boom: Low interest rates and no major upsets allow markets to rise steadily for the next 6 months for 10%+ gains.

MR or Mild Recession: Unemployment rises with hospitality etc. sectors remaining subdued with a developing Omicron virus.

SQ or Status Quo: All markets steady, significant but not rampant inflation, continued but containable COVID flare-ups.

MR is now seen as 75% more likely than **MB** as below with the Omicron virus variant poised to test world health systems at the expense of activity in other sectors, especially hospitality and tourism. The **SQ** scenario is still seen as most likely, and with a slightly increased likelihood. Probabilities for all scenarios are detailed below:

PROBABILITIES ON THE WORLD FINANCIAL STATE FOR THE NEXT 6 MONTHS

Scenario	Pairwise Judgment	Consistent Reciprocal Matrix				Eigenvalues	Probabilities	Percent Probabilities	
		D	MB	MR	SQ			Current	Previous
D	1.00	1	1/3	4/21	4/63	0.059170	0.04	4	5
MB	3.00	3	1	4/7	4/21	0.177510	0.12	12	14
MR	1.75	21/4	7/4	1	1/3	0.310643	0.21	21	20
SQ	3.00	63/4	21/4	3	1	0.931928	0.63	63	61
TOTALS						1.479251	1.00	100	100

In the above table we first calculate a perfectly consistent reciprocal matrix using the pairwise values in column 2. These are the values in the lower triangle of the matrix in column 3 in the above table. The principal eigenvector for this matrix is shown in column 4. The normalized probabilities are then shown in column 5. These probabilities are the same as would be calculated using the minimal three pairwise judgments but serve to demonstrate the more complicated method of probability derivation. Probabilities in February have increased marginally for **MR** and **SQ**. Note that the decision-maker could replace the consistent lower triangle values in the matrix above (i.e., 21/4, 63/4 and 21/4) with pairwise values he/she considers more accurate (with corresponding changes in the upper triangle values) and derive different probabilities from those shown. Note that the consistent SQ/D value is 16 so the DM would need accurate information to change this already large value. It begs the question can a DM really differentiate between say 10 and 16 times more likely?

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