Weekly Market Insights

January 11, 2021

Market Resilience and Global Realignment

Equity Markets
To their credit, U.S. investors remained remarkably calm this past week.

The Dow, S&P 500, and NASDAQ U.S. equity indexes all closed the week in record territory. This was a remarkable show of confidence in both the American political system and where the economy is headed. Investors, both domestic and foreign, were net buyers of U.S. equities. It is well known what investors faced—horrible political spectacles, a poor jobs report, the surprising results of the Georgia runoff elections, and a resurgence of the pandemic.

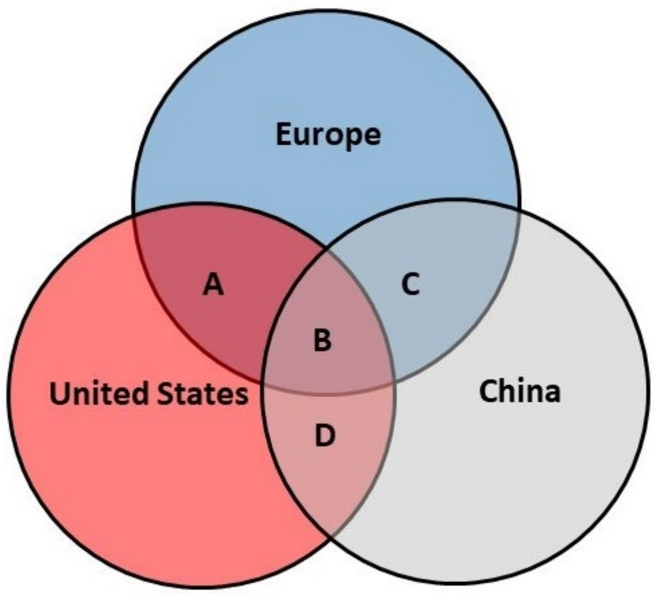
In this Sunday's *New York Times,* there was an interesting opinion piece by Jeff Sommer. He attributes the market's advance this past week to investor greed. He then points out five perfectly sound reasons for investors to remain in the market or increase positions. Perhaps he is thinking of Adam Smith's *The Wealth of Nations.* We agree that self-interest is a motivator, but self-interest and greed have very different nuances.

In any case, investors showed great faith in the system, and they appear to believe there is a light at the end of the tunnel. President-elect Biden is heavily weighting his appointments toward the moderate portion of his party. We agree that the future looks brighter. The path of pandemic continues to accelerate, but vaccines are now available and spring is in sight. Flu season will begin to slow, more government spending is now assured, and as the pandemic recedes, employment and consumer spending should accelerate. All market positives.

The DJIA closed the week up 1.6%, the S&P 500 up 1.8% and the NASDAQ up 2.4%. We can interpret this market behavior as a vote of confidence in the future of the system.

The Economy
Last week, we spent a lot of time talking about the domestic economy and the steps that can be taken to reaccelerate it in a way that benefits all. This week, we will take a look at the global economy which many analysts think is making fundamental changes. We agree, and the global economy is becoming far more important to the United States.

We start out by posting a diagram of the three most important economic entities: the United States, China and Europe.



This is a simplified picture of trade relationships. The diagram is not meant to be proportionately accurate. Some global analysts are arguing the end of the Washington Consensus[1] and globalization. The first may be true, but we doubt the second. Using the diagram, what we are currently seeing is both a reduction in B, which represents multilateral trade, and a more aggressive effort for bilateral trade agreements that are represented by A, C and D. The most important and damaging aspect of bilateral agreements is that they lead to a rebirth of industrial policy, which for all intents and purposes means protectionism.

Both globalization and the Washington Consensus have been responsible for great strides in economic well-being around the globe; however, it did not spread evenly and to some not at all. This applies to both countries and workers. There are a number of reasons. The obvious ones are governments. Even those that benefited the most did not take into account the dynamic effects of globalization. Instead, they looked at it through the lens of static equilibrium. What this means is when looking at policy options one looks at what the situation is now and what the situation will be like when all is completed. If the latter is better than the former, the trade-off is good. This, of course, ignores the good or bad that may occur in the time between the start and the end. By doing that, they did not take into account the lost jobs that would occur and skills gap that came with change. The lost jobs adjustment period is often far longer and more painful for lower paid workers, and with no or very little transferable skills, it may be hard or impossible to reemploy some. Governments with highly sophisticated economies did not plan for this outcome. The process created long-term unemployment and hardship. Are there ways to deal with this? Yes. We covered them last week, but we are suffering the effects of this failure now.

The Washington Consensus has done a great deal of good. Those economic history buffs will remember in the 1950's through the 70's, when development economics was in vogue, there was a view that for underdeveloped economies it was wise to protect infant industries. At first, it led to rapid economic growth in many underdeveloped economies, but as in most cases of protectionism, it eventually led to over production, large losses, highly inefficient production, and often corruption. The Washington Consensus ended most of that.

One of the most damaging actions that occurred was the entrance of China into the global trading partnership and the WTO. There are many reasons for this, not the least is China gives only lip service to the rules of the road, but more about that next week when we discuss China.

[1]The **Washington Consensus** is a set of ten economic policy prescriptions considered to constitute the "standard" reform package promoted for crisis-wracked developing countries by Washington, D.C.-based institutions such as the International Monetary Fund (IMF), World Bank and United States Department of the Treasury.[1] The term was first used in 1989 by English economist John Williamson.[2] The prescriptions encompassed policies in such areas as macroeconomic stabilization, economic opening with respect to both trade and investment, and the expansion of market forces within the domestic economy.

Subsequent to Williamson's use of the terminology, and despite his emphatic opposition, the phrase Washington Consensus has come to be used fairly widely in a second, broader sense, to refer to a more general orientation towards a strongly market-based approach (sometimes described as market fundamentalism or neoliberalism). In emphasizing the magnitude of the difference between the two alternative definitions, Williamson has argued (see § Origins of policy agenda and § Broad sense below) that his ten original, narrowly defined prescriptions have largely acquired the status of "motherhood and apple pie" (i.e., are broadly taken for granted), whereas the subsequent broader definition, representing a form of neoliberal manifesto, "never enjoyed a consensus [in Washington] or anywhere much else" and can reasonably be said to be dead.

Discussion of the Washington Consensus has long been contentious. Partly this reflects a lack of agreement over what is meant by the term, but there are also substantive differences over the merits and consequences of the policy prescriptions involved. Some critics take issue with the original Consensus's emphasis on the opening of developing countries to global markets, and/or with what they see as an excessive focus on strengthening the influence of domestic market forces, arguably at the expense of key functions of the state. For other commentators, the issue is more what is *missing*, including such areas as institution-building and targeted efforts to improve opportunities for the weakest in society.

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