19/19 INVESTMENT COUNSEL
Complexity to Clarity

Weekly Market Insights

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Strong Market and a Changing World

Financial Markets

United States equity markets had their best week and month in a very long time.

The Dow closed the week gaining 5.72%, the S&P 500 closed up 3.95%, while the NASDAQ closed up 2.24%. Happy as that may make investors, it may not be the most encouraging. The Dow hasn't had a month like this since January 1976, with the other indexes not far behind. Equally interesting is the order of gains. The Dow, which is loaded with large cap, industrial companies, and is often considered the most staid of indexes, far exceeded its broader and more growth weighted brethren. Both the magnitude and the distribution of gains may be telling investors and analysts something. The danger of course is that this move and its distribution is telling us nothing, but turns out to be just a dramatic correction. Nevertheless, it is positive.

Economics

As we wrote last week, markets, whether financial or not, do not act in a vacuum. Today, we look at several forces which may, in either the short or long term, be influencing the economy and markets.

The Fed and interest rates are never far from investors' minds. The financial press is beginning to play stories that the Fed, although not easing, may be slowing the rate of increase in interest rates. This view has been fostered by some differing opinions expressed by various Fed governors and presidents. This thought, whether correct or not, will move financial markets.

Another reason for U.S. financial markets to outperform is the strong dollar. A strong currency draws international investors into the U.S. markets. Also, importantly, the U.S. economy is leading most of the world in economic growth.

What we have written about so far should be characterized as short term. Far more intriguing is the long term. Alas, the longer the timeframe, the less confident one should be.

The basis of the argument for positive change over the longer term is the evolution of globalization.

Globalization is not dead, but evolving. Globalization has been going on from the beginnings of man. It doesn't end, but mutates, and it adapts to change. People enjoy writing about David Hume, Adam Smith, and David Ricardo's work on comparative advantage. This has been the basis for the gains both countries have enjoyed by U.S. trade with China. It has been a great benefit to U.S. consumers. From the beginning of U.S.-China trade, China's comparative advantage was and remains inexpensive labor. Of course, China's expertise has expanded, but labor remains an important part of the advantage. Watching China since President Xi was originally elected to his recent coronation, it is obvious that China is more and more inward looking, both economically and politically. The argument has expanded to, "the end of globalization." We argue not so, just evolution. As China backs away from global trade, there are many countries around the globe with the same attributes—cheap, efficient labor and access to raw materials as China had years ago. Examples are Vietnam and India, and, in the longer run, several countries in Africa. This change is the perfect example of what should happen with globalization. Hume, Smith, and Ricardo are resting comfortably.

There is more to the evolution of globalization than shifting trading partners. Events such as loss of trading relations, China, shrinking populations in developed countries, and rapid technological advances can dramatically change the production function even in the most economically advanced countries.

We have written about this in the past, but it bears repeating because it is germane to both our discussion of market behavior and global behavior.

Much has been written about problems facing the U.S. economy—relying on China, shrinking labor force, lowering of educational standards, and of course energy. On the other side of the ledger, the U.S. has plenty of capital, a talented, albeit vanishing, workforce, an excellent system of higher education, and the country attracts immigrants of both high and low qualifications.

We have written before about the substitution of capital for labor. We believe it is possible that any student of economics 101 will tell you, if you have an abundance of one means of production and a scarcity of other, you substitute one for the other. For the United States, it is the substitution of capital for labor. We include technological advances as capital. A great number of basic industries in the United States have not invested heavily in technology. Therefore, with both new technology and capital available, U.S. plants have the ability to rapidly modernize. This drives down costs of production and raises the marginal product of labor, which means higher wages. If this were to occur, it will raise wages and increase employment by building out new technology. This series of events would give a new life to industrial America, which, if it did occur, would lead one to think the Dow outperforming is not outlandish.

There are three things the country can do to make the above reality—spend more money on primary and secondary education and basic research, reach out to underdeveloped countries, and welcome qualified immigrants. Americans have become wary of immigrants, but we need more qualified workers. My friend Professor Jeremy Black[1] once told me that America was fortunate with immigrants. In Europe, most want to replicate their own country, while in the U.S. almost all want to embrace the U.S. and want the American way of life.

Conclusion

Investors should certainly remain cautious. There are many pitfalls for the markets and the economy, unfortunately many political. This is an effort to show some of the positives. Clearly, this is a long run view. Readers are justified in thinking this is somewhat Pollyannaish. Perhaps, but it is not out of the realm of possibility. This does not have to occur in its entirety and certainly not overnight. But, currently, there is a lot of pessimism, much of it justified. We just thought it is wise to outline what may be.

[1]Jeremy Black MBE is a British historian, writer, and former professor of history at the University of Exeter. He is a senior fellow at the Center for the Study of America and the West at the Foreign Policy Research Institute in Philadelphia, US. Wikipedia

You're Invited to a Post Election Debrief

When: Thursday, November 10th at 4 PM ET

How: This meeting will be via Zoom

Who: Our Speaker will be Dan Clifton, Head of Policy Research at Strategas Research Partners

1919 Investment Counsel cordially invites you to participate in a **Midterm Elections Debrief Webinar** on **Thursday, November 10th, at 4 PM ET,** with our trusted partner Dan Clifton, a top-ranked Washington and Tax & Accounting Policy analyst, at Strategas Research Partners.

This webinar will provide a timely window into the crucial 2022 midterm results, the upcoming lame duck session of Congress, and potential implications for investors.

Please use the link below for more information and to register for this complimentary event. Feel free to forward this invitation to family members and friends who may also be interested in joining.

Click Here to Register

If you have any questions, please contact 1919Webinars@1919ic.com.

We look forward to having you join us for this interesting discussion.

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