

# Weekly Perspectives

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## A Weekly View of Global Economies

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### North America

The US presidential election has been dominating the news this week. As of the day of writing - a day before the election results are announced - it may be appropriate to forgo any prediction of short-term market impact and focus on longer-term effects.

In the current geopolitical configuration, the United States remains unchallenged as the sole superpower. Clearly, the health of its economy and the direction of its foreign policy will have a substantial impact on the rest of the world. So, naturally, everybody will be assessing how the results will affect the markets in the months and years to come. There is not enough space to give an extended analysis, but we can start by describing features of the social and political order.

It has been observed that America is now a more divided society than for many years. George W. Bush arouses strong opinion among the electorate. People are either very favourably disposed towards the president or dislike him. There appears to be a good deal of polarisation in society, and a shrinking of the centre. So there is less room in the United States for a typical European centrist politician, such as Britain's Tony Blair. Kerry is generally regarded, not so much as an attractive alternative to the incumbent, as an anti-Bush choice.

The social and political divisions reflect trends and tendencies within society that are not easily reversed or repaired. In a climate of contentiousness and firmly-held ideological positions, reasonableness and rational argument are unlikely to flourish. In addition, people will engage in self censorship instead of offering objective analysis, for fear of offending one group or another.

The issues of Iraq and the "war on terror" dominated the election campaign, despite the Democrats' best efforts to shift focus onto other issues. This was advantageous to Bush and gave him the chance to pose as a committed war leader. The US president is, after all, the symbol of the nation, much as a king. Those who fashioned the constitution, back in the 18<sup>th</sup> century, modelled the presidency after the role of the British monarch, George III. The same symbolism but shorn of some of the autocracy. And in times of threat and impending danger people tend to rally around the king, even one they don't wholeheartedly support.

Despite appearances to the contrary, whoever wins the election is already locked into an agenda determined by earlier policy choices. It will not be possible to cut the losses and run, in Iraq. The fateful decision to invade that country, in 2003, opened up a Pandora's Box of problems. What looked easy and achievable by the Pentagon planners turned out to be complex and open-ended. All the options in Iraq are difficult ones. Abandoning the country in its current state is unthinkable, given the chaos that would ensue.

Changing direction in foreign policy is very hard to do. There are entrenched views in the bureaucracy, as well as powerful interest

groups that determine momentum. It will take a very strong and statesman-like president to go against the grain. Policy making in government is not a carefully balanced rational process of decision making. It is determined by which power-group is most persuasive in having its agenda adopted. Optimal, rational, strategic solutions are often by-passed. Such is the reality, as opposed to the idealised image, of decision making. Mistakes are often compounded, and learning from errors is a slow process.

Iraq and the "war on terror" will cost a lot more in terms of troops, treasure and possibly lost prestige. Superpower status is going to become increasingly costly and will begin to weigh more heavily on the already wide budget deficit. This has implications for the dollar, interest rates, inflation, productivity growth and profitability. There are evident risks, and we would do well to watch these trends carefully.

### Europe

German retail sales fell in September, as energy costs rose and the job market remained weak. It is a continuing story of weak domestic demand and decent export growth. Still, there is some relief on the horizon, as oil prices come down. Meanwhile, in the UK, the latest indications are that consumer spending is still fairly robust.

### Asia/Pacific

The surprise interest rate hike in China, last week, sent a few shivers around the region and, indeed, globally. But nobody has caught a cold yet. Metals and miners stocks have swung up and down, as investors remain undecided how the cycle will hit them. They are still focused on the long-term structural positives.

### Bonds

Lower oil prices and higher stock markets have helped to push up bond yields. Also, investors' expectations are that the post-election scenario will be more favourable to higher yields.

### Currencies

Foreign exchange markets are poised for a short-term dollar relief rally. There is a belief in some quarters that a Kerry victory will be more supportive of the greenback than if Bush wins. However, the fundamental structural story remains the same, whoever wins the crown.

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