

The “mild conflict”

The Cold War was a tense conflict between the United States and the Soviet Union and their allies, for the affirmation of a predominant ideology. The “mild conflict” between the United States and China is different. Understanding this difference helps to better analyze the current stage of the economic cycle.

The proletariat dictatorship in the country of Lenin, Stalin and Breznev, in which there is a planned economy, has challenged the democratic liberal capitalist model of Truman, Kennedy and Bush in the last century. With the fall of the Berlin Wall in 1989, the ideological conflict ended according to the American political theorist Francis Fukuiama, with the winning of liberal capitalism.

In the advanced economies countries, a cosmopolitan and English-speaking élite has contributed to the rapid growth of international trade. Actually, capitalism has won instead of the liberal ideology, strengthened by the faith in liberal trade. The liberal—democratic ideal was lost.

In the west countries, the *share holder value* élite has underestimated the consequences of his economic policies. The élite was convinced that the advent of capitalism would have brought the advantages and the operational costs of democracy in emerging countries, through which the global economic system would have rebalanced its surpluses, both within

and outside the country. Actually, this allowed China to develop its own capitalism, used as a mean of growth, damaging the global system. In emerging countries (with China in the center), the middle class was born, or at least developed. In the industrialized countries, the middle class has seen its purchasing power eroded. The losers’ reactions were reflected in the development of identitarian parties and in strong personalities, capable of fulfill those political figures that were missing. Trump, Salvini, Brexit are an example.

If according to von Clausewitz “war is a mere continuation of policy by other means”, according to Trump there is no need of a direct war, since he is acting within the framework that has defeated the Soviet Union: capitalism, where there are no enemies, but competitors. This is the main difference between “mild conflict” and Cold War. Nowadays, in fact, the main measure of comparison is on the economical level. Interest rates, oil price, trade tariffs are the instruments. On the other side, treasury bonds and stock exchanges performances are the instruments to measure the intensity of the challenge and the strength of the winning negotiator. Trump must win the elections and he does not have much time left, while China has more time, due to the opacity of the system.

Last year the S&P fell by 7%, while recently it gains around 11%, despite the “sell in May” (correction of more than 6,5% for the indexes among the countries on the opposite shores of the Atlantic Ocean). If Trump wants to win the elections, he could stress the trade war to the extreme during the summer, but he should also avoid macroeconomic shocks caused by lower investments. If this happens, the recovery actions necessary to have positive performances at year end could be compromised: two years of negative performances of the stock exchanges could be dangerous, even though the elections are in November 2020.

In June, the stock exchanges could bounce, since the market has already incorporated last month tensions. If central banks, especially FED, sustain Trump’s aggressive trade policy, showing signs of monetary slack, stock exchanges could be near to the end of the correction. On the other side, if they will take more time, American stock exchanges will hit another minimum followed by several ups and downs during summer. The latter scenario is as far as more probable due to the current macroeconomic data, that show signs of a slow-down. Trump, as well as the FED, have fixed a threshold, below which the macroeconomic risk would sharpening. Trump’s tweets will show us his tolerance level. According to him, 2019 should recover 2018 losses, with the addition of a further 4-5%.

In Europe, the situation is different. The strong personalities that have taken the lead, have an identity function that places them – according to their characteristics – above the capitalism logic that is reflected in stock exchanges and spreads between government bonds. There may be the need of a significant conflict, maybe among Italy, Brexit and European Commission – and therefore with the markets – prior to deal with a global reasoning that considers the interdependencies among the EU members. The focus is on Italy and Germany. Salvini could delude himself that he could beat the markets. Germany, whose Deutsche Bank stock hit their historical minimum value below 6 euro, could try a recovery that could be dangerous for Europe’s equilibria. This would open a discussion over the “mild conflict”.

China could wait until the election of a new president of the United States and take time. On the other side, China knows that in order to obtain this result, in addition to countermoves on trade tariffs, should also consider monetary devaluation dynamics. Therefore, the “mild conflict” would become more dangerous. The focus is on the Hong Kong dollar, whose central bank is forced to almost run out of reserves in order to maintain the Hong Kong dollar pegged to the US dollar.