John Dessauer Investments, Inc.

John Dessauer's market review and update as of Wednesday January 12, 2022

There is something missing in all the outlook 2022 articles I have been reading. There is a powerful economic force beyond the control of Washington politicians and the Fed - that is the global currency market. Trillions of dollars are traded each day on the global currency market. So far, the dollar has been strong. The DXY, a gauge of the dollar versus half a dozen other rich world economies, is up about 7%. A broader measure of the dollar versus 26 of America's trading partners is also up nicely. That is unusual. In normal times the currency market responds to relative interest and inflation rates. For the last year interest rates in the U.S. have been at record lows. Yes, those rates have been slightly better than interest rates in Europe and elsewhere. But that in my view is not enough to justify the strong dollar. The pandemic is what has distorted economies and the relative attractiveness of the dollar. The United States has been a more reliable source of growth than other countries. We have been able to recover much faster than just about anywhere else.

Surprisingly, the Chinese yuan is an exception. The yuan has kept pace with the dollar because there has been more money flowing into China than out.

The strong dollar has been a major plus for the U.S. economy. Not only has that made U.S. debt more attractive to investors, but it has also helped mute inflation by making imports less expensive.

The question now is: how will the currency market behave as the pace of U.S. economic growth slows and inflation remains stubbornly high? The answer will depend on how the U.S. economy behaves and how the Fed responds. The Fed has already announced a pull back in the monthly bond buying. And that opens the door to higher interest rates if need be.

When it comes to currency trading all things are relative. This means that the fate of the dollar is as much dependent on what happens in other countries as it is on U.S. performance. For example, if the eurozone were to raise interest rates that could be a game changer for the dollar. Imagine a shift in bond buying by foreign investors. If they cut back on buying U.S. government bonds because government bonds in Europe became more attractive, that could mean difficulties financing the huge U.S. government debt.

And U.S. political good intentions are making international trade more complicated. Years ago, I visited a region in China that is home to the Uyghurs, a mostly Muslim ethnic group. Back then China was treating the Uyghurs harshly. The Uyghurs complained that they were no longer allowed to have guns. That meant a major change in their lifestyle. Hunting was no longer possible. Instead, they became goat herders. In addition, there have been reports of the Chinese forcing the Uyghurs to work in factories under poor conditions. Of course, China denies using forced labor anywhere. But American human-rights defenders have prevailed. The U.S. Congress has passed a law called "The Uyghur Forced Labor Prevention Act." It bans the import of products from the region of Xinjiang in China on the presumption that they are made with the forced labor of Uyghurs. Goods from Xinjiang can be brought to America only if it can be proven that they were not made with forced labor. That is just about impossible because China does not allow the proper inspection of factories and supply side providers.

The law will make it difficult for American businesses because key components often come from China. For example, it will be very difficult to find a new source of nitrogen heterocyclic compounds that are critical in the manufacture of cancer treatment drugs. In addition, China is a huge market for American made products. American companies that export to China will have to be very careful that they do not show support for the new American law. Intel made that mistake and suffered a nasty backlash from Beijing. Intel had to apologize to Beijing for its positive comments about the new law.

The worst aspect of the new law is that it simply isn't likely to work. Goods from Xinjiang can still be sold elsewhere in China or to other countries that are not so critical of China's labor practices.

The human-rights folks in the U.S. are celebrating what they see as a victory with the new law. But the reality is very different. The new law will not stop Beijing from abusing the Uyghurs. Beijing can work around the new U.S. law without suffering politically or economically. In my view the new law will disrupt critical parts of the supply chain without any benefit to the Uyghurs. That is hardly a victory for human rights.

Closer to home the December jobs report was a huge disappointment. The U.S. economy added 199,000 new jobs last month. Economists and investors were expecting 400,000 or more new jobs. On the plus side the unemployment rate fell from 4.2% to

3.9%. That looks inconsistent with the disappointing new jobs report. But it simply is the pandemic which has made the labor department's work more difficult. The result is more volatility in the jobs reporting. The underlying economy is strong, and the December jobs report may well be revised upwards. In addition, the Omicron variant has been making some people sick and scaring others. The evidence however is that Omicron is not as deadly as earlier versions and those who get sick are not as sick and recover fairly quickly.

The stock market pulled back a bit after the December jobs report. However, that looked more like investors being cautious than a precursor to a major sell-off. We will soon be in fourth quarter earnings season. If the reports are as good as expected, stocks will likely resume their upward trend.

I will have the next market and update for you one week from today on Wednesday January 19, 2022

All the best,

John Dessauer