
Weekly Market Flash

Grand Theories and Mundane Realities

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The sweep of history always looks neater when observed from a distance. We speak with confidence about the natural and human forces that drove the transition from medieval to modern Europe, or the fall of Rome, or the rise of Meiji-era Japan. Easy divisions of the flow of time help us mark our story on this planet. Our distance from them allows us to overlay the actual events of those times with grand theories as to how they came about.

Big Government...

Even recent history seems to afford us the simple narrative. At the end of the Second World War the US stood alone as a global economic superpower. Through a combination of far-sighted benevolence and self-interest, so we tell ourselves, we sponsored the Marshall Plan to rebuild a war-torn world, exercising tolerance to our former enemies as they reconstructed and reformed their devastated lands. A thirty-year period of worldwide economic growth followed under the Bretton Woods agreement, the framework fashioned by the great and good at the eponymous New Hampshire resort in 1944.

Governments were the lead agents in the world of Bretton Woods. Here in the US government's share of the total economy, already at a high level following the reforms of the Depression-era New Deal, grew throughout the 1950s and 1960s. The Cold War gave rise to the military-industrial complex. The Eisenhower administration spent billions on national infrastructure, including the interstate highway system. Social welfare programs and the Vietnam War drove budgets ever higher in the 1960s. Businesses from manufacturing to communications to finance were highly regulated. At one point the top marginal tax rate was 92 percent.

...To Small Government...

The postwar Bretton Woods framework finally fell apart in the 1970s, and from its ashes rose the Phoenix of privatization, globalization and deregulation. Big corporations went from being the villainous Scrooges of popular culture to being glorified. In the age of "greed is good" the shareholder was dominant, the government was the problem, and all the riches of the world were there for the taking by whoever could come up with the best cash flow model. Regulation was not needed because the market itself was self-regulating. Human self-interest – greed itself – would correct and reverse any excesses.

The advent of the commercial Internet in the 1990s seemed to put a final definitive stamp on this era, ensuring that not only businesses could roam the globe, but so could people. National borders were becoming quaint relics of a distant past, clunky obstacles to one global village, with low taxes and cheap consumer goods for all. It was, in the popular mindset, the literal end of history. Until it suddenly wasn't.

...And Back Again?

This simple narrative of the postwar world now has a new chapter in support of an old theory. The theory is the idea of multi-decade economic wave cycles. In one cycle private enterprise and free markets loom large; in the next they are eclipsed by Big Government and spending and regulations, and then back again in a never-ending oscillation. The next big shift is now at hand, according to the theorists. In the last twelve months alone we have spent over \$5 trillion in fiscal relief and stimulus to combat the effects of the

coronavirus pandemic. Now President Biden and his administration are rolling out the details of a \$2 trillion infrastructure program, potentially followed by another \$1 trillion in other forms of social spending. Taxes, in particular corporate taxes, are set to rise. The big problems of our era – climate change, public health, income inequality, education – are all in clear focus for government to solve.

The idea that this is hard evidence of the next big turn in the wave cycle theory is almost irresistible. Theorists will draw direct analogies with the previous transition from big-government Bretton Woods to small-government Thatcher/Reaganism. Just as the 1970s was a decade of stumbling through the fog after Nixon took us off the gold exchange standard in 1971, so too were the 2010s a decade of groping through a slow-growth, central bank-funded miasma after the globalization-era Masters of the Universe lost their invincibility during the 2008 financial crisis. Now, say the theorists, the new era is at hand.

Pop Goes the Narrative

Except that reality is always much messier than theory. What we are going to be seeing in the coming weeks and months is not any kind of smooth, inevitable transition to a new world of big government. We will instead be witnessing the mundane reality of negotiations, compromises and fudges – the world of actual policymaking. Yes, the Biden administration is making a big bet on what it thinks is the right way to address the many pressing problems we currently face as a nation. But that infrastructure program has miles to go before it becomes law. The administration will have to deal not only with the near-certainty of no help from Republicans to divisions within its own side. Outcomes here are far from certain.

It has always been thus. It is worth remembering that the Marshall Plan – that sweeping reconstruction plan that made those first twenty-five years of postwar growth possible – barely passed through Congress. A couple more votes from recalcitrant isolationists would have torpedoed the deal, and the world would very likely look a lot different today as a result. It's worth remembering that Ronald Reagan's victory in 1980, heralding the era of small government, was due more to the (for Jimmy Carter) unfortunate timing of a recession and the Iranian hostage crisis in 1980 than it was to any sweeping natural force of history.

Theories of history are fun for salon chatter and late-night college dorm bull sessions. But we are still far from having our current era written into the history books as a definitive narrative. For now, it's all about the gritty sausage-making of policy, one day at a time.

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