

2022 Economic Outlook

Stephan: Hello, welcome. It's great to have you joining us and let me take the opportunity on behalf of our entire organization to wish everyone a Happy New Year. I'm Stephan Bourbonnais of iA Private Wealth. And it's my pleasure to welcome you to our 2022 economic outlook.

As we begin a new year we welcome new opportunities for personal growth and for financial success. But we also face renewed uncertainty and challenges, as we're thinking about increased market volatility, rising inflation and obviously a continued pandemic-driven uncertainty as the Omicron variant of COVID-19 spreads at record rates.

If 2020 was the year of the virus, 2021 will be remembered as the year of the vaccine, but also as a year where we saw strong market returns both in Canada and in the U.S. market. So as investors, what should we expect of 2022? At iA Private Wealth, our advisors and our partners have the benefit of having access to a vast resource of experts, which includes an industry leading economic research team led by Sébastien Mc Mahon who joins me now to discuss the micro-economics and the market outlook for 2022.

Sébastien, welcome, thanks for joining us.

Sébastien: Thanks for having me and Happy New Year to everyone out there.

Stephan: We were talking about the fact that 2021, we saw strong market return in the U.S. and Canada. You've also been quoted to say that 2022 will be the year of uncertainty. Where are we now in the business cycle and can we expect the economy to continue to do well in 2022?

Sébastien: Yeah, that's a great question. So the good news is that we're still early in the business cycle. The easy part is behind us, the part where you just rebound from the recession. You have strong growth. This is behind us. But as you can see, the chart that I brought here, we still have very strong growth, so this is a picture of the business cycle that you have there, so the higher the line, the stronger the growth, and the lower the line of course, the stronger the contraction. So we are still at the very elevated growth. We're coming off a little bit which is normal, but in 2022, we're very much looking at again about 4% growth for real GDP in Canada, the U.S., Europe, strong global growth.

So we're still good. We still have a lot of good years ahead of us in this cycle.

Stephan: And how much of a risk factor could COVID play in 2022?

Sébastien: COVID is still very much an important risk. With Omicron there's still a lot of uncertainty. Right now we see the number of cases has not peaked yet around the world. And it's a risk for the business cycle in the sense that the distribution of the vaccine has been unequal around the world. So some countries will be recovering faster than others, so it creates some friction around this business cycle, number one.

And number two, China has a very strict zero COVID policy, so when Omicron starts to be more of a problem in China, how will they react? How will it impact the global supply chain? This should be the main macro risk for 2022.

Stephan: We have to talk about inflation. I mean it's been a top topic obviously in 2021. As customers we are feeling the impact of inflation. Were you surprised to see inflation soar that way in 2021, and how is that – can we explain the acceleration in the inflation?

Sébastien: Sure, so we were expecting inflation to pick up in 2021 to be honest, but we were surprised by the speed and the strength of this inflationary burst. So we saw it, and as you can see, the chart that I brought, it comes mostly from the prices of goods. So of course inflation is in the price of goods and services, so we shifted the way that we spend, less spending on services because of the restrictions. You go less to the restaurants. You spend less on services. So there's more pressure on goods right now, and this is where the inflationary pressure is.

So pressure on commodity prices, when you shut down the lights, as we did on the global economy in 2020, and you turn them back on again, it takes awhile for everything to get back in sync. So it's more about pressure on the supply chain on the side of goods, that is explaining this inflationary pressure.

The good news is that maybe we're near the peak of the inflation rate right now.

Stephan: So a lot of it I think is tied to the situation of the pandemic, but what do you see in terms of inflation for the years to come?

Sébastien: Yeah sure. So maybe we're near the peak. Will it be in Q1, in Q2 but we're nearing that peak. After that we should just have the base effects, so just the comparison, remember that inflation is a change in prices between now and 12 months ago. So as we move forward in 2022, the comparison effects will be helping pushing inflation down. So at some point this year, we expect lower inflation than right now. Will it be 3%, 4%? But still a lot of uncertainty around that.

But then if you look forward in time, wage pressures are something that's starting to happen right now, more in the U.S. than in Canada, but we're expecting it to come here too. So if you look 10 years forward, I would say that the break evens right now are calling about 2.5% on average inflation over the next 10 years. I think that's about right. And I think that next decade will see inflation being more often above central bank targets than below, like we've seen in the last 10 years.

Stephan: The stock markets have performed well over the last past few years, and it seems like they're getting pretty expensive right now. Should we moderate our expectation in terms of returns for 2022?

Sébastien: Yeah of course you should moderate your expectations. I mean Stephan, you know this. Markets don't give 20% return with very low volatility forever. So these years were exceptional, the last two years let's say post March 2020. So over the next few years, we are expecting global equities to return about 5 to 8% on average per year, so the traditional long-term trend.

But you will need to be picky, so active management is going to be key, because some markets right now like the U.S., are much more expensive than other markets like Canada for example.

Stephan: 2021 was a challenging year for bonds. I mean we rarely see a negative year for bonds as we did in 2021. Interest rates are remaining very low. Is it still worth holding bonds in our portfolio?

Sébastien: Yes, sure. You always need to hold bonds for diversification purposes. As you mentioned, negative returns in 2021, but if you look at history, the global bond index has been negative only four times since the mid 1970s. So for equities it's much more often than that that we have negative years.

So for diversification purposes, you need that, but you need to be active within bond management in 2022 with being active on duration, being picky in credit. So you need that to add value, because with central banks looking to tighten, and to tighten pretty quickly, early in the year, the Fed, the Bank of Canada were talking about March or April, it's very possible that we have for the first time in modern history, back to back negative years for once.

Stephan: And where would you look at investing money in 2022? What are some of the opportunities you're seeing?

Sébastien: Yeah, global Ex-U.S. equities I think is the way to go. So emerging markets will be interesting at some point, negative last year. China was negative so we know that China wants to reflate, wants to get the economic cycle going. That could help emerging markets. Also we know that the Fed is looking to tighten maybe in early 2022, maybe looking at the month of March for the first rate hike. When the Fed starts tightening, usually that's negative for the U.S. dollar and money starts to go elsewhere around the world. So that helps Europe, it helps emerging markets, as I said. the TSX, as we can see on the chart, I mean had a very good year in 2021, the TSX. But when you look at the relative valuation versus the U.S., we're pretty much as cheap now as we were at the peak of the .com bubble.

So we think if you have a long-term horizon, 3-5 years ahead, being more heavily invested in Canada versus the U.S. I think that's a very interesting opportunity that is presented here.

Stephan: Yeah, any final thoughts or recommendation you could share with our clients?

Sébastien: Yeah, sure. It's always important to stay invested, to keep your emotions in check. Timing, the market is hard, so being active means going where the opportunities are, moving the money around, but trying to time when the market could be under pressure, and trying to time when to get back in. It's tricky, even for people like us who manage \$13 billion dollars. I mean you need to stay invested. You need to stay diversified, and the key is to be patient and always play the long game.

Sébastien: Great advice. I couldn't agree more. And thank you for your insightful perspective. And let me take a moment to reiterate the enduring value of professional financial advice. Research has shown that the surest way to thrive on life's complex and sometimes bumpy road is to create a comprehensive wealth plan with an independent, professional advisor, who has the intimate understanding of your unique goals and your unique objective.

When you work with an iA Private Wealth investment advisor, you have a true partner who's fully dedicated to your success, both for today and for many years to come.

So thank you for joining us, hope you've enjoyed the presentation. See you next time.



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