

2022 Economic Outlook – Light at the End of Another Tunnel

[Soft music plays]

[Benjamin Tal, Managing Director and Deputy Chief Economist
CIBC Capital Markets]

2022, so what should we expect? Early in this madness, we looked at the trajectory of the economy and we said it's going to be like a zigzag economy. The economy will be dancing to the tune of the virus, and that's exactly what we are seeing. We can discuss the numbers, but the trajectory in many ways is predictable.

[Empty airports in winter.]

Basically, the winter is bad.

[A time-lapse image of a bustling airport.]

The summer is much better. We have seen it in 2020, 2021, and we will see it in 2022.

[A man in a mask walks down a winter street. A man in a mask picks up a winter jacket in a store. A close view of an empty luggage carrier at an airport. A food courier in a mask walks down a winter street.]

Now we are, unfortunately in the winter, it's going to be a long winter and we see some seasonality when it comes to the virus. So, we know that the first quarter of the year will be actually negative.

[A bird's eye view of people jogging on a bridge in spring.]

The spring will be better.

[High angle view of a crowded beach. Time lapse images of bustling malls.]

The summer will be on fire as people start spending this mountain of cash that they are sitting on. So, it's very predictable. We know that it's going to be very complicated, and we know that in the case of Canada, it's going to be more complicated than, let's say, in the U.S. and even Europe, because we reach capacity in our health care system much faster than most other OECD countries.

[Images of busy hospital hallways.]

And therefore, we have to introduce restrictions much faster. And that's why Canada has been lagging the U.S. economically. We will see the same in 2022, but it will be mostly in the first half of the year. In the second half, especially this summer we are going to see actually very strong growth. Overall, you sum it up, and we are talking about GDP growth in 2022 of about 4%, 4.5%, starting from a very low base in the first quarter, as we go through the winter.

[Inflation]

In the background, we have inflation. And we have to watch this inflation. And let me tell you one thing. Nobody knows where inflation will be six months from now.

[Low angle view on a Canadian flag attached to a government building. Low angle view on an American flag attached to a government building.]

And when I say nobody, I include the Bank of Canada and the Fed in that. Everybody's pretending, but nobody knows. So, clearly there is a risk here and the source of this inflation is coming from wages. The labor market is very tight. Vacancy rates are extremely high. We cannot find people.

[A shipping barge docked in ice. An empty warehouse.]

We have supply chains that we are all aware of. And we have this kind of spending that will be coming in the second half of the year.

[A woman shops for shoes on her phone followed by images of people online shopping on their computers.]

When it comes to supply chain, it's very important to understand that it's mostly a demand led shock. Listen to this. In the U.S., this huge increase in spending on goods, and it's easy to spend on goods;

[A woman rides an exercise bike in her living room.]

You press a button, and you get your exercise bike, it's very easy.

[Images of multiple people parachuting through the sky followed by someone landing on the ground.]

This extra spending is equivalent to basically overnight, parachuting 75 million people, extra people, into the U.S. and the minute they land, they start spending. This is a demand shock, and even a normally functioning supply system will have difficulties facing this demand shock. And this is not a normally functioning supply system. So, I think it's reasonable to assume that it will take a while.

[The exterior of the Bank of Canada building. The exterior of the St. Louis Federal Reserve building.]

The Bank of Canada, the Fed underestimated how long it would take. Now it's clear that this supply chain issue will be with us until late 2022, so inflation will be there.

[Interest rates]

Wages are rising, and that's something that will lead to higher interest rates.

[The exterior of the Bank of Canada building.]

Now the market is pricing in no less than six or maybe five moves by the Bank of Canada, namely 125 basis points in 2022. That's a significant increase. That's what the market is expecting. I believe that the market is wrong on that because I think that the Bank of Canada is aware that the number one enemy of the economy is overshooting. You don't want to raise interest rates too quickly. Every economic recession over the past 50 years was helped, if not caused by monetary policy error in which central bankers raised interest rates too much.

[The crest of the Bank of Canada building. The Bank of Canada building at night.]

Therefore, we believe that the Bank of Canada will be more muted. They will move only by three times, namely 75 basis points in 2022. They will continue to go in 2023. Overall, we see the bank rates rising from 25 basis points to maybe 2% by the end of 2024, but a very gradual trajectory as opposed to a very quick trajectory, what the market is expecting now.

[Stock and bond market implications]

This, of course, has major implications for the stock market and asset allocations.

[Computer generated imagery of market data. A bank of computer monitors featuring market data.]

Clearly, the bond market is not your friend at this point. I believe that rates will be rising, reflecting inflation expectations, and reflecting the rebound in the economy in the second half of the year. Therefore, in the stock market, clearly you have to be very choosy.

[Market data on various tablets and screens.]

And I would focus on growth-oriented stocks. I would focus on stocks that are actually going to pay back investors, dividend paying stocks like banks, utilities that will benefit from this environment.

[An aerial view of a hydro electric dam. A low angle view of bank towers.]

Banks will benefit also from higher rates. The spreads will improve. That's another positive, and we believe that all this is under one big assumption that Omicron is basically a transition from a pandemic to endemic. And by spring, summer of 2022, although COVID will not disappear, we will learn to live with the virus, basically coexist with it as an endemic as opposed to pandemic. And this, of course, has implications for the market.

So overall, economic growth, mostly in the spring and the summer in 2022, it will be strong. I believe that inflation will last in 2022 above target. Therefore, the Bank of Canada will be raising interest rates, but not as quickly as anticipated by the market at this point. This has implications for not the bond market, but the stock market. I believe that when it comes to the stock market, we are going to see growth-oriented dividend paying stocks outperforming in this environment of rising interest rates. As well, I believe that service-oriented companies will be benefiting due to the fact that the consumer, especially in the spring and the summer, will be spending this mountain of cash that they are sitting on at this point.

[This video is provided for general informational purposes only and does not constitute financial, investment, tax, legal or accounting advice nor does it constitute an offer or solicitation to buy or sell any securities referred to. Individual circumstances and current events are critical to sound investment planning; anyone wishing to act on this document should consult with his or her advisor. All opinions and estimates expressed in this video are as of the date of publication unless otherwise indicated, and are subject to change.

™The CIBC logo is a trademark of Canadian Imperial Bank of Commerce (CIBC).

The material and/or its contents may not be reproduced without the express written consent of CIBC.]

[CIBC Logo]

[The CIBC logo is a trademark of CIBC, used under licence.]