Canaccord Genuity Wealth Management

Staying the Course: Look Forward with Confidence

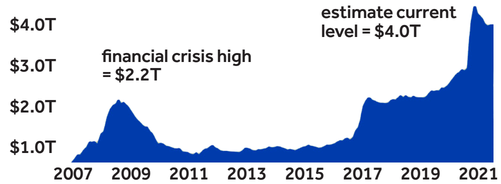
The year 2021 will likely go down in the record books as an impressive one for equity markets. As such, some are asking if further upside can be had as we look ahead to 2022. While it's never possible to predict the direction of the markets in the near term, there may be reasons to support a continued upward climb:

Still room for growth! Let's not forget that in 2021, Canada's economy struggled through recovery mode. Our economy remained shut down much longer than the U.S., and recent growth has been hindered by factors including supply chain bottlenecks, labour supply issues and continuing pressures as a result of new variants. These are expected to normalize as full economic recovery takes course. For instance, labour issues may have been exacerbated by generous pandemic stimulus cheques; workers are likely to head back as this support runs out. Building upon this economic recovery, the potential for expansive fiscal measures, such as President Biden's ambitious infrastructure plan in the U.S., may help to support continued growth.

An accommodative Federal Reserve. Many central banks have been highly accommodative and have expressed patience with their policies. While many have indicated that increasing rates are on the horizon, we suggest that rates are not likely to rapidly rise. Monetary policy is likely to play an ongoing role as nations grapple with higher debt-to-GDP ratios as a result of pandemic stimulus — they still need to service this debt, and with higher interest rates, the cost of carrying this debt becomes larger. Markets are also forward-looking in nature and expectations for rate increases in 2022 have been largely priced in. It may also be worth remembering that the timing is still uncertain: when the Fed started to taper in 2013 after the financial crisis, investors expected the first rate increase within the year, about a full year before it actually happened.[1]

Significant cash on the sidelines. Many companies built substantial cash reserves for insurance throughout the pandemic; by some estimates, the largest non-financial companies have a record $7 trillion of cash on their balance sheets.[2] Given continued strength in earnings, these companies may look to unwind their reserves to fund projects and investments to drive growth. Similarly, households are sitting on record amounts of cash, giving confidence that consumer spending will be unleashed as supply constraints are resolved.[3] The amount of assets in money market funds also remains at highs, suggesting potential for this to be injected into higher-return equity markets.

Significant Cash on the Sidelines
Money Market Funds Assets Under Management



Sources: Office of Financial Research, Morningstar Direct, 01/01/2007 to 03/31/2021.

Inflation: deflate your concerns. While many pandemic-related headwinds that have pushed inflation higher are expected to moderate in 2022, even if more persistent inflation is here to stay longer, there is no clear risk to equity markets. History suggests that there isn't a distinct pattern between high inflation and equity market returns. It's worth remembering that staying invested in the equity markets can be one of the best inflation hedges. History shows that stocks beat inflation over the long term. As one market analyst recently suggested: "deflate your inflation concerns!"[4]

Stock Market Returns During High Inflation Years

Inflation	S&P 500 Returns	Year	Inflation	S&P 500 Returns	Year
14.4%	5.2%	1947	8.5%	-8.4%	1946
13.6%	31.7%	1980	7.9%	23.7%	1951
11.3%	18.5%	1979	7.7%	5.7%	1948
11.1%	-25.9%	1974	7.6%	6.5%	1978
10.9%	19.2%	1942	6.5%	-7.0%	1977
10.3%	-4.7%	1981	6.2%	-14.3%	1973
9.1%	37.0%	1975	6.1%	20.4%	1982

Source: awealthofcommonsense.com/2021/10/inflation-vs-stock-market-returns/

The Bottom Line

There are, no doubt, many challenges ahead, but their eventual outcomes on the markets are often difficult to predict. Don't let them stop you from staying the course. Look forward with confidence!

1. www.wsj.com/articles/narrowing-yield-gap-in-treasurys-signals-worries-over-fed-growth-11635586201; 2. www.cnn.com/2021/08/17/investing/cash-companies-balance-sheet/index.html; 3. www.wsj.com/amp/articles/americas-cash-might-stay-on-the-sidelines-11632423163; 4. www.wsj.com/articles/deflating-your-inflation-investing-fears-11635519805

Compliments of John W. Warnke — Canaccord Genuity Wealth Management

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