Wednesday, January 12, 2022

Frances Donald, Global Chief Economist, and Global Head of Macroeconomic Strategy, Manulife Investment Management

The third issue I'm having is figuring out central bank policy. This is always hard. This is always a challenge. But in the past, what we would see is that central banks that had dual mandates, whether they're spelled out or not, would see that employment and inflation moved in the same direction. So you would have, you know, job growth rising at the same extent that you would have inflation, so you knew that the next move would be a hike. Or you might see the opposite, which is that you would see job growth decelerating and prices declining, and then you knew that central banks would be cutting interest rates.

The problem that we have now in Canada and the US, is that, of course, inflation is surging – as I said, the bulk of this not related to monetary policy at all – but growth is actually still very, very tenuous. In Canada because we've gone to another lockdown; in the US because they have a highly dysfunctional labour market and there are massive amounts of supports that are being withdrawn from the system on the government side. So central banks need to start raising interest rates, but doing it in a way that does not slow growth too dramatically just as we're getting to the point where the economy is re-accelerating. And I don't know what central bankers are going to do.

Here's my base case. My base case is that both the Bank of Canada and the Fed hike rates twice this year. That's less than the market is pricing. The market is pricing in four in the US, and five or six in Canada. The problem I have is that I think the data is going to be really challenging in the first half of the year. And while inflation stays high, growth will actually start decelerating for a lot of the reasons that we've talked about. And how central bankers respond to that is really challenging. Canada has a single mandate: inflation. And they've said that they really want a hike soon, but can they do that when, you know, 60% of the economy is in lockdown? I don't think so. Maybe, maybe not.

The Fed, well, the Fed's about to see inflation slow really dramatically back towards 2% and they have a massive, massive problem in their labour markets. They have a huge shortage of workers. How do they address the situation? I think they're going to move very slowly, much more slowly than markets expect, which is also one of the reasons why I'm not rolling out the fixed income space at all. At all, at all, at all. Because there is a lot of hawkishness priced in; a lot of short duration positioning here that, well, maybe is going to turn out to be a little bit too much sentiment.

Follow the Private Wealth Podcast on www.manulifeprivatewealth.com or contact us via manulifeprivatwealth@manulife.com for more information.

and may be superseded by subsequent market events or for other reasons. There is no assurance that such events will occur, and if they were to occur, the results may be significantly different than those shown here. This recording may contain forward-looking statements about the markets, model portfolios and expected future performance. Forward-looking statements are not guarantees of future performance. Forward-looking statements involve inherent risks and uncertainties, both about the individual portfolio components and general economic factors, so it is possible that expectations, forecasts, projections and other forward-looking statements will not be achieved. Manulife Private Wealth cautions you not to place undue reliance on these statements as a number of important factors could cause actual events or results to differ materially from those express or implied in any forward-looking statement made herein. These factors include, but are not limited to, general economic, political and market factors in Canada, the United States and internationally, interest and foreign exchange rates, global equity and capital markets, business competition, technological changes, changes in laws and regulations, and catastrophic events. Before making any investment decisions, Manulife Private Wealth encourages you to consider these and other factors carefully. Should you have any questions, please contact or ask to speak to a member of Manulife Private Wealth.