Economic Commentary

Fourth Quarter 2021

Rise of Omicron Leads To Heighted Restrictions

The emergence of the Omicron variant at the end of the quarter was swift and far-reaching. Despite the fact that fully vaccinated people are now contracting the new virus, the ongoing strain on the health care system continues to be driven by the unvaccinated. Stricter measures have once again been put in place, which will have a negative impact on first quarter economic activity. The hope is, despite the widespread nature of the virus, that the effects will be short-lived and the strain diminishes as quickly as it appeared.

Housing Drives North American Recovery

Home prices increased 20% annually in both Canada and the U.S. during 2021. A pandemic shift in housing preferences has occurred, with a migration towards suburban living, as more employers are adopting the flexibility for employees to work-from-home. Demand continues to be strong while supply is tight leading to affordability issues, particularly for first -time buyers.

The labour market continues to add jobs, with unemployment rates in both Canada and the U.S. improving steadily. Despite the large number of unemployed people, companies are finding it difficult to source skilled labour. In the U.S., there are approximately 1.6 jobs available for every unemployed person. Early retirement and migration out of low-paying service jobs have contributed to this disconnect.

Elevated Inflation Likely to Persist in 2022

Elevated inflation is the key factor impacting financial markets and monetary policy expecta-tions heading into 2022. U.S. Federal Reserve Chair Powell indicated that inflationary pressures due to supply chain bottlenecks have been larger and lasted longer than anticipated. He has removed the term transitory from his statements when referencing the higher-than-expected inflation levels. Inflationary pressures are likely to remain elevated for an extended period of time.

U.S. FED To Begin Tapering

The U.S. Federal Reserve and Bank of Canada continued with their hawkish stance during the quarter. The elevated and persistent rate of inflation remains the key concern. The Fed announced that it will now end it's asset purchase program in March rather than June. This opens the door for administered rates to move higher shortly thereafter. Markets are now expecting three rate increases in 2022. In addition, the Fed noted that it would be appropriate to begin reducing its balance sheet, once it begins to increase interest rates.

The BOC signalled that it will begin increasing interest rates early in the year, possibly during the first quarter. Markets are pricing in five interest rate hikes in 2022.

Equities Finish Strong, Bonds Fluctuate

Equity markets finished the year on a strong note with the TSX posting a 25% return for 2021. Investors are anticipating that the negative impact of Omicron will be short-lived. Bond yields fluctuated during the quarter, as the yield on shorter-dated maturities increased while the yield on long-term bonds declined. Expectations for more rate hikes hurt the front end of the curve, while investors in longer-dated bonds took comfort in the fact that central banks would do their part to reign in inflationary pressures.

Key Metrics

Indicator	Value	Chg Q4	Chg 1Y
S&P/TSX Composite	21,222.84	6.5%	25.2%
S&P 500 (USD)	4,766.18	11.0%	28.7%
iShares MSCI EAFE ETF (USD)	78.68	2.8%	11.5%
USD/CAD	$ 0.79	0.3%	0.8%
WTI Crude ($/bl))	$ 75.21	0.2%	55.0%
GoC 10Y Bond	1.43%	-8 bps	75 bps
GoC Deposit Rate	0.25%	0 bps	0 bps
Cdn CPI YoY	4.7%	0.3%	4.0%
US 10Y Treasury	1.51%	2 bps	60 bps
Fed Funds Rate	0.25%	0 bps	0 bps
USD CPI YoY	6.8%	1.4%	5.4%

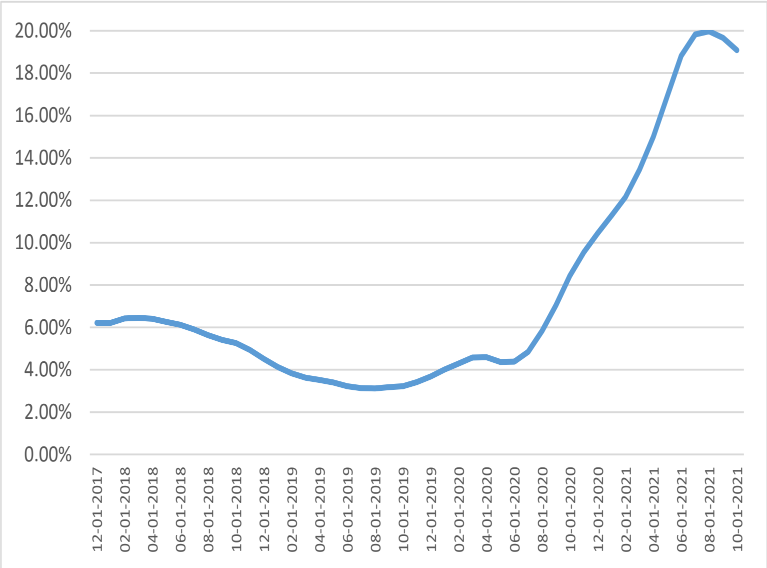
Top Themes

Swift emergence of Omicron variant leads to heightened restrictions

Elevated inflation likely to persist into 2022

U.S. Federal Reserve to begin tapering bond purchases

Top Chart: SP Case-Shiller U.S. Home Price Index (YoY %)



Source: Bloomberg, Lincluden