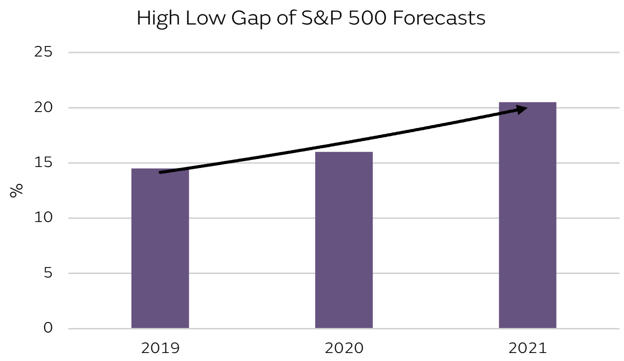
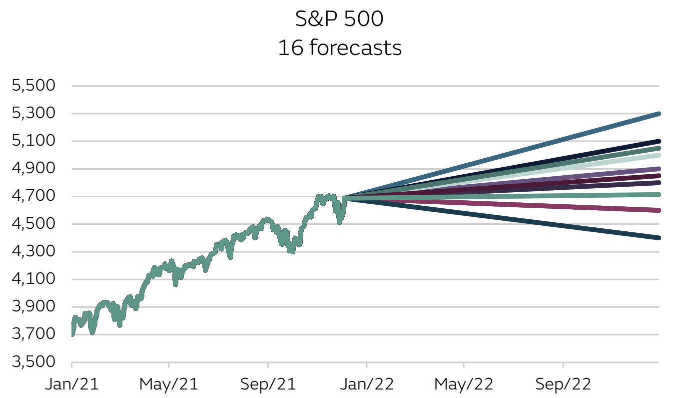
December 2021: time to ditch the 2022 outlook

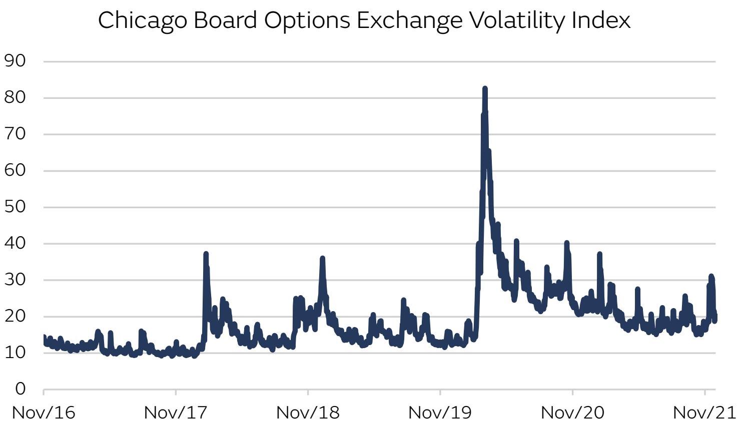
It's December, the traditional time to roll out the 2022 economic outlook and markets forecast. However, based on the belief in the primacy of markets, market forecasts are telling us we don't know where we are headed in 2022.

Indeed the level of uncertainty, as measured by the high-low gap in target equity performance, as polled by Bloomberg, is the second-widest in a decade. Not only that but there is wide direction dispersion between those who think the market will go up and those who think it will go down. The uncertainty gap has also significantly grown this year despite prognostications that we are closer to back to normal – clearly not.





One might expect uncertainty such as this would to be picked up in measures of volatility but, while the default volatility index, the VIX (The Chicago Board Options Exchange Volatility Index), clearly stepped up at the beginning of the pandemic it has consistently fallen since then and is now below the value of 20 generally accepted as the stress-free threshold.



So what's going on? It's the economic and policy backdrop, stupid. (Credit: James Carville, 1992).

In September last year the Fed told us that so long as consumers' and businesses' expectations of future inflation remains stable, it will hold interest rates near zero until inflation is "on track to moderately exceed 2% for some time" and until the labor market reaches conditions associated with maximum employment. Inflation of course has exceeded 2% for almost all of 2021 and in October this year the Fed finally conceded that "transitory is a dirty word".

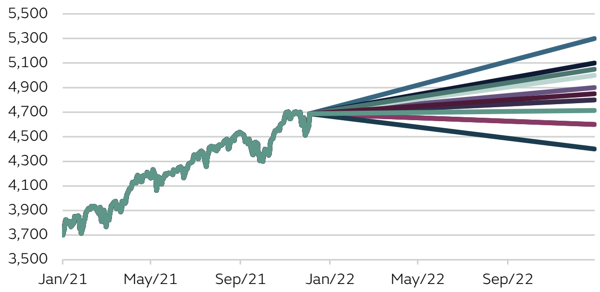
Meanwhile the Bank of England has been going back and forth: signalling a rate rise in November and then promptly reversing course following strong jobs data and inflation peaking at 4.2% and then this week conceding that inflation is persistent when it hit a 10-year high of 5.1% and becoming the first Central Bank to actually raise rates.

Indeed the whole notion of forward guidance governing central bank monetary policy has been subsumed by a move back to data-dependency. Given the range and dispersion of current forecasts for 2022 that seems appropriate. Indeed so appropriate that we believe that “market consensus” is a dirty word.

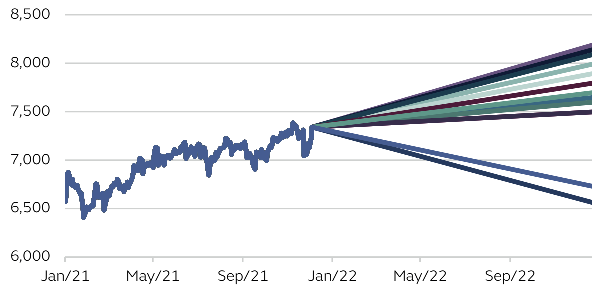
Let’s have a look at those ranges of forecasts as polled by Bloomberg.

Equities may go up, they may go down.

S&P 500
16 forecasts

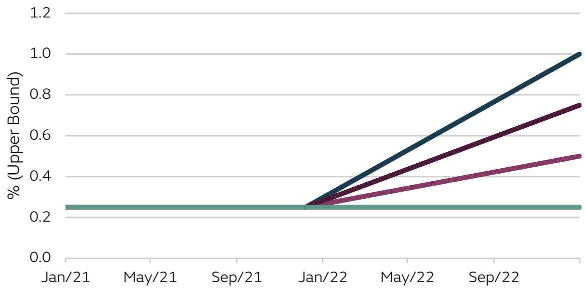


FTSE 100
14 forecasts

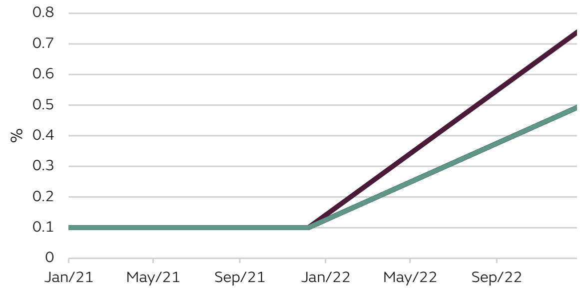


No one seems to think that short term rates are going down.

Fed Funds
41 forecasts

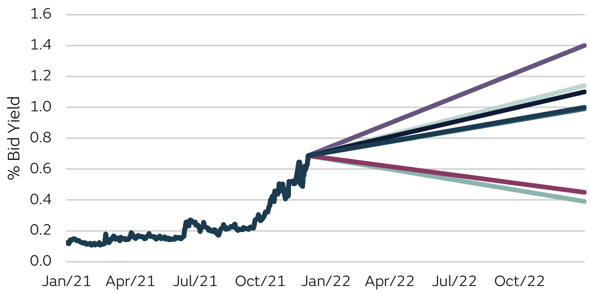


BOE Bank Rate
44 forecasts

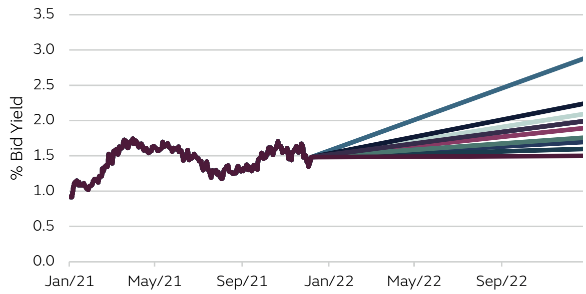


But term rates could go either way and the curve could flatten or steepen.

US 2 Year
50 forecasts

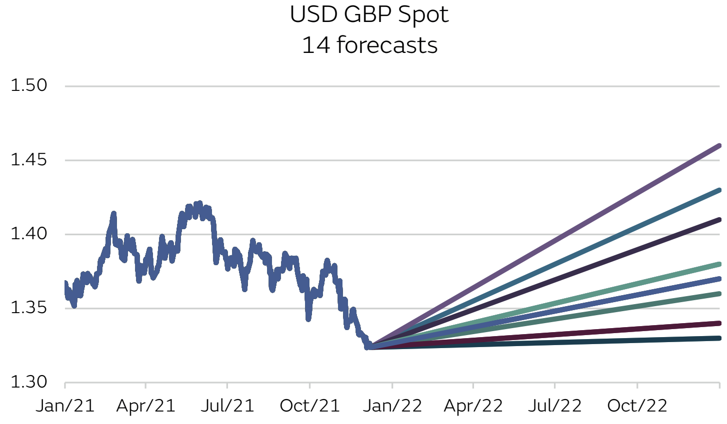


US 10 Year
59 forecasts

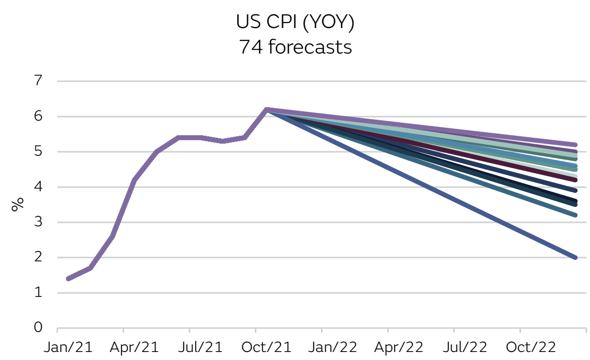


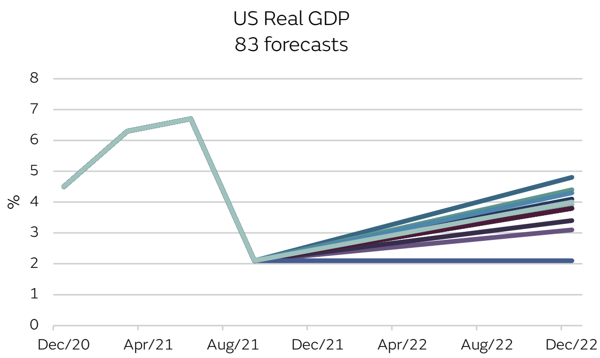
Source of charts: Bloomberg

There seems to be a view that Sterling won't weaken further but most forecasts seem anchor-biased to 2021's range.

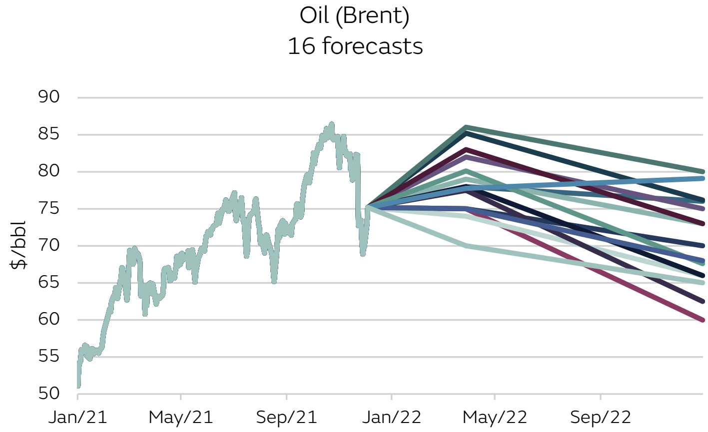


Inflation forecasts remain above the Fed target (for almost all) but without damaging real GDP growth forecasts.





But those real GDP growth forecasts don't carry over to forecasts for higher oil prices which remain 2021 range-bound.



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Feel free to contact us at info@gibam.com. Meanwhile, Happy New Year to all.