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Inflation will remain central to investment strategies in 2022

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Inflationary pressures, rising interest rates, and economic slowdown are expected to dominate 2022. On the stock market, this context is likely to favour companies that are able to generate growth while maintaining profit margins, as well as businesses that stand to benefit from inflationary factors.

After the global economy bounced back and prices rose sharply in 2021, investors now face a year marked by more persistent inflation, rising interest rates, and growth returning to a lower level.

Deemed temporary just a few months ago, inflation seems to have settled in for the long-term, fuelled by factors including energy prices and shortages in several business sectors. The consumer price index measured in OECD countries[1] continued to rise in November to 5.8% – its highest level in 25 years.

"While we expect inflation to fall in 2022, it could prove more persistent than people tend to admit," comments Frédéric Leroux, a member of the Carmignac Strategic Investment Committee. "Prices could continue to rise for some time before losing momentum, and inflation could be driven by a number of longer-lasting factors."

The potential risks looming large in 2022 include a shutdown of the Chinese economy linked to the country's "zero COVID-19" strategy, a possible continuation of commodity price rises and a geopolitical crisis in the Ukraine that would have knock-on implications for the cost of gas.

This inflationary environment will prompt more central banks – tasked with regulating economic activity – to raise their interest rates and push up those applied to borrowers and savers.

"For years, the US Federal Reserve acted on the basis of investor behaviour. Now, inflation is the driving force behind the actions of the Fed and also set to determine what the European Central Bank will do," says Frédéric Leroux. "But the central banks will be trying to preserve growth at the same time as combatting the problem of inflation. It is an extremely tricky task that will require a lot of skill."

Favourable factors

And this is the crux of the matter, since rising interest rates, coupled with possible new variants of COVID-19, the sharp increase in commodity prices, and the current Chinese economic slowdown, could weigh heavily on the global economy. We estimate that global growth could slow by 4% this year after a 5.5% increase in 2021.

"The start of the year will be lacklustre because of the Omicron wave," predicts Raphaël Gallardo, Chief Economist at Carmignac. "Worldwide economic growth will slow in the first three quarters before rebounding in the last three months of the year fuelled by the measures China is likely to introduce to kickstart its economy."

On the stock market, this backdrop of inflationary pressures and economic slowdown justifies the adoption of a defensive approach. It could favour companies that are able to secure growth while maintaining profit margins in a period of inflation by passing on higher costs to the end customer. Investors may also turn to issuers with less exposure to the economic cycle, such as those selling essential goods and services (food, personal care, health care, etc.).

In parallel, rising energy prices could support the energy sector, while banks stand to benefit from higher interest rates. Moreover, China remains a vital market over the long-term since new measures are expected that will support the world's second-largest economic power.

Against this backdrop, active management[2] could allow investors to stay ahead of the game. "It's never easy to spot the perfect time to invest, but a context like the one we anticipate could generate opportunities for those who know how to seize them. However, as a long-term investor, our investment horizon is much longer than a few months," notes Kevin Thozet, a member of the Carmignac Investment Committee.

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[1] Source: OECD

[2] Active management entails selecting the financial assets (equities, bonds, currencies, etc.) that will generate the best performance in relative terms and buying at the right time. By contrast, passive management involves seeking to follow a stock market index.