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Winners and Losers of the Post-Pandemic Landscape

LUXEMBOURG & WARSAW | Here's the good news: this year should see economies stabilise. Moreover, more risky assets come back to focus with markets expecting cyclical industries equity to yield better returns. And now the bad: high inflation takes a toll on personal finances and rentability of some financial instruments, observe Jerzy Kasprzak and Marcin Stosio from Q Securities.

There's much room for optimism in 2022. "After turbulences, we are gradually returning to a textbook behaviour of the economy," said Marcin Stosio, head of equity capital markets (ECM) at Q Securities, a brokerage house and depositary for alternative funds. Textbook meaning economy that is cyclical and interventions of central banks and fiscal administration are limited to a minimum.

It was not the case over the past two years as governments were pumping tremendous amounts of money into the real economy and resuscitating companies in the hardest-hit industries that would otherwise go bust. Some were also helping the common people by introducing government-backed job support schemes.

But now everyone's paying the price for all the spending with surging inflation that in Europe reached 5% on average, Eurostat reported in February.

"The two years of giving away public money helped contain – to some extent – the negative economic impact of the pandemic on the society. But as consumers were widely limited in their habits due to lockdowns, as soon as people were allowed out, many went on a spending spree," Jerzy Kasprzak, deputy CEO at Q Securities, said. Moreover, the 'back-to-shopping-malls-excitement' was such that higher prices were barely off-putting for all those hungry to buy goods or pay for services they were deprived of due to lockdowns.

"Because of backlogs in supply chains, costs of raw materials and energy swelling, and increased consumer demand, prices for goods, services and utilities started to climb. But, with savings waiting to be spent, many tacitly accepted the increases," said Jerzy Kasprzak.

Slow central bank reaction

Now comes the question about how governments had the money for the unexpected spending in the first place. "The funds did not materialise from some hidden vaults. To be able to spend so much in such a short period, governments needed to swell public debt levels," Q Securities deputy CEO said.

Recovery plans were widely fuelled by borrowed funds. The government debt-to-GDP ratio increased from 77.2 % at the end of 2019 to 90.1 % at the end of 2020, Eurostat informed at the end of last year and noted that it was "the highest in the time series". And debts will sooner or later need to be serviced.

"One way is for governments to raise taxes," Marcin Stasio said. At the same time, inflation comes in handy, as it consumes at least a part of the money governments would otherwise need to repay.

So instead of using their key tool – and deciding to raise interest rates – central banks might choose to hold off. "We are already seeing some reserve, as central banks – including the ECB – have not yet decided to take action and so far, are keeping rates at an unchanged level," Kasprzak said.

It might be tempting to keep interest rates at a level lower than the market conditions suggest. Still, however, at least some rate change is expected.

Real economy versus pandemic stars

Despite 2022 being expected to be a year of stabilisation – with possible lockdowns and production halt shocks no longer as disruptive as during the first pandemic waves – Jerzy Kasprzak and Marcin Stosio expect volatility in financial markets.

Even if interest rates will only moderately increase, it will automatically lead to reduced spending and subdue economic growth. "Higher borrowing costs negatively impact real estate prices, as fewer people can afford a mortgage, and lead to a drop in the value of different types of debt instruments," said Marcin Stosio, Q Securities head of ECM.

On the upside, inflation is positively correlated with the value of equity and precious metals, at least historically.

"Most stocks bounced back after the crisis; now comes the time when selection becomes more important than allocation. Stock market stars from the lockdown might be priced lower post-pandemic than real economy stocks," Marcin Stosio said.

Q Securities experts expect positive returns from cyclical industries whose services or goods are in demand during economic growth.

Key takeaways:

• 2022 is expected to bring economic stabilisation after coronavirus.

• High inflation should trigger an interest rates hike, but central banks might want to stall taking action in a bid to alleviate heavily indebted governments.

• Winners of the changing conditions are to be sought among cyclical companies producing dispensable goods and services whose stocks typically fluctuate depending on the economic cycle.

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