Here’s How Investors Can Beat the Coming Rate Hike

Description

Over the past week, Canadians saw the unemployment rate in the country drop drastically, which is fantastic if you’re an average worker. The same cannot be said for investors, however. Historically speaking, a low unemployment rate is a leading indicator that the economy will enter a recession and stocks will decline in value.

The rationale for the unraveling of the good times is that many workers will be putting in 40-hour (or more) work weeks with the income to purchase additional goods that companies don’t necessarily have the capacity to produce. With more people working, the demand for products and services will increase, which will push share prices higher. The downside for stock prices will be that expectations far outweigh capacity, which very often leads to a correction in overall share prices.

Due to the very low unemployment rate, the expectations from almost all Canadian big banks is that the government will again be increasing the prime interest rate. The next interest rate announcement is scheduled for January 17 of this year. As it is highly probable that interest rates will rise, the very real danger is that the economy, which is currently performing extremely well, could see a gradual pullback, as the average Canadian will be forced to spend more income to service their variable debts.

We’ve seen it all before and it never gets easier.

It spite of the past rate hike having very little effect on the broader economy (and share prices), this rate hike will be the third increase since July of 2017. It may therefore start to dampen the strength of the economy as the middle class will be stretched once again.

With revenues for lenders increasing, the best way for investors to benefit from this rate hike will be to buy shares in companies that lend consumers money. For those seeking lower risk alternatives, shares of Canadian big banks such as **Royal Bank of Canada** (TSX:RY)(NYSE:RY) will be among the best choices, as the company will be able to increase rates of the currently outstanding variable loans while securing their own rate of borrowing through fixed-rate guaranteed investment certificates (GICs) offered to clients.

On the more aggressive side, shares of B-type lenders such as **Equitable Group Inc.** (TSX:EQB) are currently offering investors a dividend yield of almost 1.5% in addition to a book value that is nearly equal to the current share price. As interest rates continue to rise, the company will be primed to increase revenues based on a consistent loan book.

Although higher interest rates will act as a headwind for the general economy, those who invest in common shares need not worry, as there are many effective means of finding increased profits throughout the next phase of the economic cycle.

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