If CERB Becomes UBI, What Happens to the Stock Market?

Description

The Canada Emergency Relief Benefit (CERB) program could be coming to an end soon. Now, public debate has moved on to the idea of a universal basic income (UBI). While a UBI is far from a reality right now, investors should consider the implications of such a move on the stock market to be better prepared.

Here's how a UBI could impact stocks and alter the economy.

Basic spending

By definition, UBI is expected to be just high enough to allow citizens to meet basic expenses. This means the cost of rent, food, clothing and utilities would ideally be accounted for.

A UBI would boost consumption of these basic necessities, which could bolster companies that provide essential goods. Basically, the program could act as an indirect stimulus package for the most essential stocks on the stock market.

However, as this amount is paid out to everyone, some of the cash could wind up in assets and savings as well.

Stock market drivers

Middle and high income recipients of UBI are much more likely to invest rather than spend their spare cash. As basic income flows into the real estate and stock markets, asset valuations could rise much higher.

We've already seen the impact of CERB on the Canadian stock market these past six months. Millions of Canadians poured benefit payments into the stock market to create additional income and speculative gains. UBI could make these lofty valuations and surging asset prices permanent.

What about inflation?

Critics of UBI often argue that government stimulus measures expand the national debt pile, decrease the value of the currency and increase inflation.

In theory, all of these fears are justified. However, the evidence seems to suggest otherwise. Since January 2020, the value of the Canadian dollar is down just 1% against the United States dollar. Total consumer price index (a measure of inflation) has actually declined from 2.4% in January to 0.1% now, according to the Bank of Canada.

In other words, the CAD-USD exchange rate and inflation haven't exploded despite the fact that Canada has handed out benefits worth 15% of the economy over the past six months.

Betting on potential winners

If this trend continues and UBI is implemented, certain segments of the stock market could emerge as clear winners. Investors should focus on high-growth essential stocks such as **Dollarama** (TSX:DOL).

Not only is dollarama an essential business, but it's also proven to be a recession-proof one that directly benefited from higher CERB spending. The stock is up 10% year to date and an impressive 40% since late March.

Despite this surge, the stock is trading at a price-to-earnings ratio of 28, as the company saw a noticeable spike in earnings during the crisis. The next crisis could bring another version of CERB or a permanent UBI, both of which will help Dollarama stock move higher.

Even without government stimulus, the company has plenty of opportunity for growth. Acquisitions of smaller companies in developing countries could help Dollarama expand its footprint. Over the long-term, this could be one of the best performing growth stocks in the country.

Bottom line

As CERB is phased out, there's growing chatter about a permanent UBI, potentially boosting the stock market and especially benefit stocks such as Dollarama.

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Date
2025/07/26
Date Created
2020/09/04
Author
vraisinghani