Rising Inflation: Don’t Panic. Here’s a Good Inflation Hedge

Description

Inflation is on the rise.

According to *StatCan,* the CPI was up 1.1% in February compared to 0.62% for the full year 2020.

1.1% inflation isn’t exactly an unprecedentedly high level — the Bank of Canada generally aims for 2%. But the fact that it’s increasing should give you pause. As of the most recent reports, nation-wide unemployment was 8.2%. 599,000 more Canadians were unemployed in March 2021 compared to February 2020. Yet prices are already starting to rise. As people get back to work, then, we may see levels of inflation that people aren’t prepared to cope with.

Inflation is already rising

The 1.1% inflation rate reported for February isn’t alarmingly high. But rising prices could affect you differently than it affects the “average” person. It all depends on how your spending breaks down. If you spend a large share of your income on gasoline or household appliances, then you’ll feel more “inflation” than most. Those goods rose more than others in February and may continue rising in the year ahead.

Some think inflation could rise more

If inflation were to continue at 1.1%, that wouldn’t be a big deal. Salaries usually rise with the prices of goods — although not always in perfect proportion — and people can prepare for *expected* inflation.

It’s *unexpected* inflation that’s a problem. If the prices of commodities were to inexplicably increase 50% overnight, salaries wouldn’t immediately adjust. It would take time for the economy as a whole to respond to the increasing prices of staples.

This is why many institutions, including the Bank of Canada, are worried about inflation in the year ahead. Canada ran a record deficit ($380 billion) for the 2020-2021 fiscal year, and reduced interest rates to record lows. Those two taken together tend to be a recipe for high inflation. So far, that hasn't been the case. 1.1% inflation is *up* from the 2020 pace but is lower than the Bank of Canada's 2% target. It's when people get back to work that the system will truly be tested. Then we'll have both more money in the system and more of it circulating at stores. The possibility of unexpected inflation is therefore very real.

Real estate: A good inflation hedge

If Canada's rising inflation rate has you worried, there is one good hedge you could consider: real estate.

You've probably heard about Canada's red-hot housing market. If you're younger, you may have spent some time bemoaning how expensive houses have gotten. Be that as it may, Canadian house prices have been outpacing inflation for well over a decade. In other words, homes have provided ample inflation protection. If you have the means, you might want to consider buying a rental property to get some extra income going.

If you can't afford a house at the moment, you could consider a REIT like **Killam Properties REIT** (TSX:KMP). Killam is a residential REIT that rents out apartments across Canada. Like housing, its rental income typically increases every year. In 2020, that wasn't the case. Rents went down despite house prices going up, because so many people were out of work. But rent should start rising once more once employment levels pick up. Once that happens, Killam will be able to increase its rental rates ever so slightly every year, providing growing earnings that serve to hedge investors against inflation. No, it won't provide the practical benefits that owning a house would. But a REIT like KPM could be a worthy alternative if you're looking into real estate as an investment and nothing else.

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