Inflation Is a Danger to Retirees

Description

By now we've all heard the story about inflation: *"Sure, prices will rise, but your salary will rise too, so it's nothing to be concerned about."* Indeed, mild to moderate inflation can be healthy, a sign of economic growth. But there's one group of people who do tend to get hit hard by inflation:

Retirees.

Many retirees live on fixed incomes. Specifically, pensions that are not indexed to inflation. Canada's CPP is inflation-indexed, but it doesn't pay much. Many employer-sponsored pension plans simply pay a set amount per year. Typically, it's a percentage of a person's best few earnings years. For people earning a fixed salary for the rest of their lives, inflation is a daunting prospect. In this article, I'll explore the effect that inflation has on retirees–and what can be done about it.

What the U.K.'s experts say

In 2012, the U.K.'s Institute for Fiscal Studies (IFS) did a study on the effects of inflation on various elements in society. As predicted, retirees were among those hardest hit. Not only did their fixed incomes fail to keep pace with inflation, but the kinds of goods they bought experienced *more* inflation than those bought by younger consumers.

For example, retirees spent a large share of their income on food, which was among the categories that rose the most in price in the period studied. This time around, fuel is seeing the biggest rise in price. Retirees typically spend less on gasoline than other consumers do, so our current inflation scare isn't quite the same as what was seen in the 2012 study. However, retirees remain vulnerable to price increases in many categories, including rent, prescription drugs, and utilities.

How to protect yourself

If you're a retiree worried about the effects of inflation, you may be wondering what to do. There's always the option of going back to work, but depending on your health, that may not be an option. So the real question is, *what can you do with your savings to combat the effects of inflation?*

One thing you can do is invest your money. By investing in inflation-resistant stocks, you can grow your money so it keeps pace with inflation. Take **Royal Bank of Canada** (TSX:RY)(NYSE:RY), for example. A bank like RY makes money by collecting interest on loans. Those loan interest figures tend to be influenced by Bank of Canada interest rates. The more cheaply the Bank will loan money to RBC, the more cheaply RBC will lend it out to clients.

What does this have to do with inflation?

Well, when inflation spirals out of control, central banks tend to respond by raising interest rates. The higher the interest rate, the lower the inflation rate, because with high-interest rates, you have fewer people borrowing money, and therefore fewer people spending it. When interest rates rise, banks like RY earn higher profit margins on their loans. They also *pay* more interest on savings accounts, but the effect on loans tends to predominate. So, bank stocks could be one type of investment with a shot at beating inflation.

There are two other types of stocks worth mentioning here: energy stocks like **Suncor Energy** and REITs like **NorthWest Healthcare Properties REIT.** Oil and real estate are two assets that tend to go up in price when inflation is roaring. Suncor and NWH make money off these assets, so it stands to reason they'll thrive in a high inflation environment. If you look at their stock charts, they've been rising this year. While that in itself doesn't make them great investments, they could be good stocks to look at when building your retirement portfolio.

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