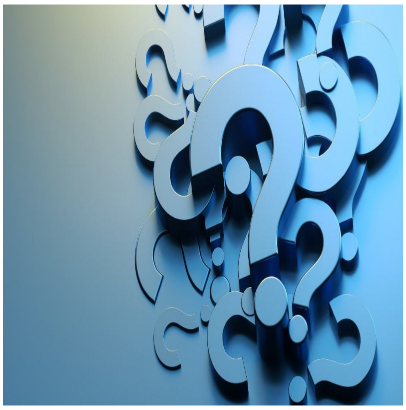

Inflation Hits 5.7%: Could it Go Higher?

Description

The official inflation rate hit 5.7%, according to the latest data published by Statistics Canada today. That's the fastest pace since 1991. The cost of living is rapidly accelerating, making everything from gasoline to rent less affordable.

This is also an invisible tax on your wealth. Here's how investors can prepare for the gradual loss of purchasing power.

Invisible tax

A loss of purchasing power is an invisible drag on your portfolio. At the current rate of inflation, your stocks would have to deliver 5.7% in dividend yield or annual capital gains *just to retain purchasing power.* Most stocks don't offer such returns.

However, some stocks retain their value better than others and can outpace inflation. These stocks could serve as an effective hedge against the rising cost of living.

Inflation hedges

Companies with pricing power or hard assets can withstand inflation better than the rest. For instance, a gold mining stock should outperform during inflationary cycles as the value of this precious metal soars. **Barrick Gold** stock is up 28.5% year to date, which has already offset much of the inflation we're seeing.

Other hard assets such as real estate, equipment, and raw materials could also serve as safe havens. At the moment, energy and fertilizer stocks seem to be riding this wave.

However, the best hedge could be companies that have pricing power. High-quality businesses that offer essential services, such as **Fortis**, could raise prices in line with cost pressures. This means their margins and earning power is stable regardless of the economic cycle. Fortis stock is flat year to date, but the company offers a 3.5% dividend yield and 5-6% dividend growth, which offsets inflation.

Contrarian bets

In the current environment, most investors are risk averse. The market is actively seeking ways to preserve capital, which means growth isn't the top priority.

However, I believe this could be the best opportunity to make a contrarian bet on growth stocks. Undervalued growth stocks could face some pressures for the next few months or years, but over time, they can outstrip inflation by a mile.

Take **Constellation Software** (TSX:CSU) for instance. This enterprise software giant has lost 10% of its value year to date. In fact, the stock price has been rangebound since August 2021. However, the company's underlying fundamentals are still strong, and growth is expected to be robust for the foreseeable future.

Constellation Software stock has delivered a compounded annual growth rate of 34% over the past 16 years! That rate is significantly higher than the decline in purchasing power over the same period. In simple terms, blue-chip tech stocks create value, despite market cycles.

Now that the stock is facing pressure, long-term growth investors have the opportunity to buy it at a reasonable price. The stock currently trades at a price-to-free cash flow ratio of 26.3.

Bottom line

Investors could bet on hard assets and commodities to offset the rising cost of living. However, I prefer to make a contrarian, long-term bet on robust growth stocks like Constellation Software.

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