Inflation Compensation

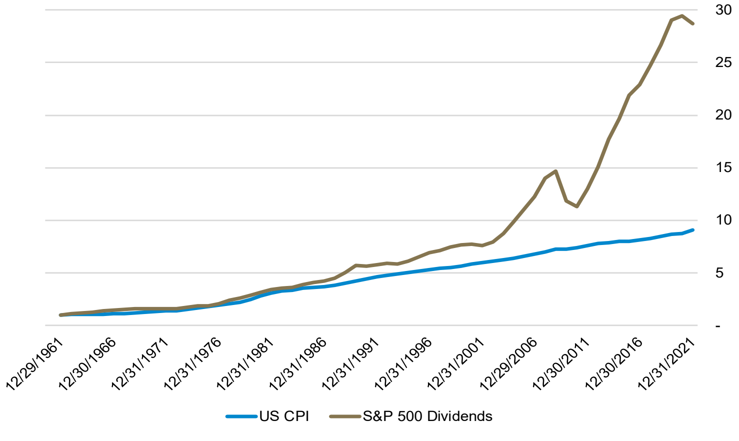
It has been a difficult year for consumers, with rising prices for food, energy and durable goods rippling through the economy. Thankfully, investors with exposure to dividend-growing corporations can shield themselves from some of this inflationary pain by collecting rising income from these stocks. While the ability to surmount inflationary pressures will vary by company, spanning a range from weak to robust, some firms, such as Walmart and Costco, are well placed as inflation beaters. These two leading retailers stand to gain market share, as their low prices become even more attractive to shoppers facing rising grocery costs with every passing week. A smaller portion of the market offers a direct connection between dividends and inflation, such as major UK utility, National Grid, paying a dividend formulaically linked to UK consumer prices. Others benefit from pricing power that can protect shareholder profits, even as costs rise. Pepsi, owner of Frito Lay potato chips, Quaker Oats snacks and Pepsi beverages, is a great example. Currently facing higher ingredient costs, shipping expenses and wage increases, Pepsi has responded with higher prices as an offset; this pricing power has allowed Pepsi to pay a rising dividend for the past 50 years.

To be sure, not every company is able to offset the headwinds of inflation as deftly as National Grid or Pepsi. Regardless, over the entire stock market, dividends have a proven history of matching and surpassing inflation in the economy. The table below compares inflation to stock market dividends over the past 60 years, a stretch including more benign periods as well as the frothy years of the 1970s, the last major spell of inflation. While there are periods when dividends do well to just keep pace, including years when the economy is in a capital investment phase, over the entire stretch, dividends have risen at 5.8% annually, just over 2.0% higher than the pace of inflation.

	Last 60 Years	2011-2021	2000-2010	1990-2000	1980-1990	1971-1981	1961-1971
US CPI	**3.7%**	1.9%	2.4%	2.7%	4.1%	8.4%	3.1%
S&P 500 Dividends	**5.8%**	8.6%	5.6%	2.8%	5.4%	8.0%	4.3%

Sources: US Bureau Of Labour Statistics, Factset, December 31, 1961 to December 31, 2021

While this difference might not sound like much, the benefit to dividend investors becomes sizeable over time. Inflation may have brought the price of a $1 item to just over $9 since 1961, but $1 of dividends produced by the stock market has grown to nearly $29 over the same span. A reasonably diversified equity portfolio will likely contain a mix of stocks with differing attributes, but when inflation starts to exact a toll on consumers, the portion invested in high-quality, dividend-paying companies should help collect a growing income stream as an offset.



Sources: US Bureau Of Labour Statistics, Factset