



Straight TALK

HELPING YOU MAKE SENSE
OF YOUR INVESTMENTS

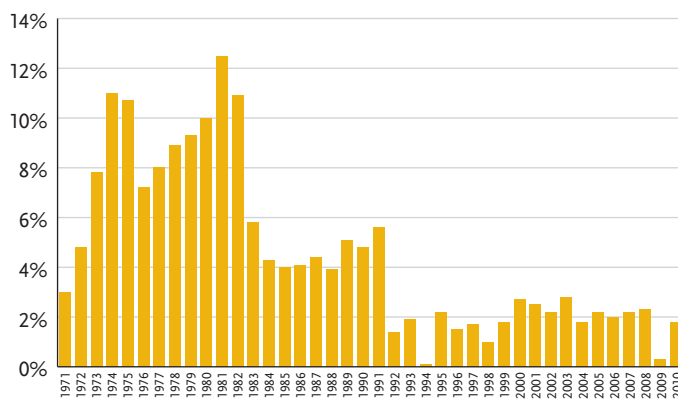
The Inflation Effect: How will it impact you?



Inflation can affect many aspects of our lives, from the cost of food to how much we need to spend on a new car or a new house. Though you may not notice over the short term, inflation can have a substantial negative effect on the value of your purchasing power and of your investment portfolio over the long term. Investors need to be aware of the risks and know what steps they can take to protect their portfolios from inflationary pressures.

Inflation is, in a nutshell, the rate at which the price for goods and services, and therefore the cost of living, rises. A chief measure of price inflation is the inflation rate, which is the annualized percentage change in a general price index (normally the Consumer Price Index) over time.

Although it hasn't over the past several years, inflation can rise quite dramatically, as the chart below illustrates. For example in 1981, inflation rose 12% from the previous year.



Source: Statistics Canada



What are you doing after work?®

So far in 2011, inflation is beginning to rise in emerging markets, particularly in Brazil and India, and central banks in many developing countries are attempting to curb inflation by hiking interest rates and other policy measures. Closer to home, inflationary pressures in the U.S. and Canada are relatively insignificant and interest rate hikes will most likely be minimal for the rest of the year. Yet, Canadians cannot avoid a rise in inflation and an increase in interest rates is likely at some point in the near future.

The main culprit of higher prices is the rising cost of raw materials and basic commodities. This ultimately leads to higher prices for food and clothing. Costs of everything from corn and cotton to oil and copper are all steadily rising, eventually trickling down to the costs of basic goods like bread and T-shirts.

THE EFFECTS OF INFLATION

When making investment decisions, many investors do not take into account the adverse effects inflation can have on their portfolios over time. This is especially important for RRSPs when investments are made to provide retirement income 10, 20 or even 30 years from now. For example, if annual inflation is at 3%, in just 10 years, investors will have to withdraw over \$130 from their RRSP to purchase the same products that cost \$100 today. And in 20 years, that retiree will have to withdraw \$180 to maintain today's lifestyle.

THE RISING PRICE OF DAILY NECESSITIES

Postage	Loaf of bread	Car
1970 – \$0.06	1970 – \$0.24	1970 – \$2,500
1990 – \$0.39	1990 – \$1.29	1990 – \$9,440
2010 – \$0.57	2010 – \$2.59	2010 – \$29,105
2030 – \$???	2030 – \$???	2030 – \$???

Source: Library and Archives Canada

Source: www.wife.org

Source: www.wife.org

PROTECT YOUR PORTFOLIO

Fortunately, there are a number of strategies you can employ and specific securities you can purchase to help protect your investments from the impacts of inflation and rising interest rates.

Inflation-linked bonds (ILBs) – these guarantee that an investor's returns are not reduced by inflation because the bond's principal amount is adjusted to reflect the changes in inflation, so they are worth considering when inflation is present or expected to rise. They can be purchased directly or as part of a diversified fixed income mutual fund.

Floating-rate notes (FRNs) – these are attractive when interest rates are expected to rise because the interest rate of the bond is linked to the market's interest rate (raising rates are a key measure used by central banks to stave off future inflation, so inflation and rising rates are often discussed together). When interest rates rise, the bond's interest payment (coupon) increases, protecting the investor. In contrast, bonds with fixed coupons lose value when interest rates rise.

Equities – Another way to beat inflation is to invest where your money will grow faster than the rate of inflation. History has proven that stocks outperform inflation over time. Over the past 20 years, the average inflation rate in Canada has been 2% while the average annual performance of the S&P/TSX Composite Index was 9.7%.¹ By investing in dividend-paying stocks during an inflationary environment, you can receive a steady income stream that can help outpace inflation as well as have growth potential. Keep in mind that investing in common stocks involves a higher risk tolerance than fixed-income investing.

Commodities – Commodity prices and inflation are closely linked, so investors who have a higher risk tolerance can capitalize on rising commodity prices during periods of rising inflation. The commodity sector has promising long-term growth potential as global expansion, particularly in emerging markets, drives demand for oil, copper and other commodities.

¹ Statistics Canada, Bloomberg, as of March 31, 2011

* You cannot invest directly in an index

Talk with your financial advisor to determine the right strategy to help you mitigate the impact of inflation, grow your portfolio over time and manage risk.

Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund investments. Please read the prospectus before investing. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated.

