



# YOUR FINANCIAL FUTURE

Your Guide to Life Planning

November 2011

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### Should You Prep Your Portfolio for Inflation?

The dreaded "I" word -- inflation -- has been cropping up more frequently lately, largely due to escalating commodity prices, which are pushing up consumer prices, both in the United States and abroad.

### Calculating Your Retirement Needs

Less than half of American workers have tried to figure out how much money they will need to accumulate for retirement. Here are some suggestions to help you do your own calculations.

## Should You Prep Your Portfolio for Inflation?

Economists and market watchers have been warning investors about the prospect of increased inflation since the housing bubble burst in 2007.

The dreaded "I" word has been cropping up more frequently lately, largely due to escalating commodity prices, which are pushing up consumer prices, both in the United States and abroad. At the beginning of 2011, the inflation rate stood at a paltry 1.6%. By May, it had more than doubled to 3.6%. And this could be just the start of a longer-term inflationary cycle.<sup>1</sup> With an improving economy and soaring federal deficits, many experts feel that prices in the United States will inevitably pick up their pace even further.

### Inflation Rates Around the World (as of May 31, 2011)<sup>2</sup>

Country	Rate
Brazil	6.6%
Canada	3.3%
China	5.5%
Egypt	11.8%
Germany	2.3%
India	9.4%
Japan	0.3%
Russia	9.6%
United Kingdom	4.5%
United States	3.6%
Venezuela	22.8%

### Staying Ahead

For investors, staying ahead of inflation means choosing investments that are most likely to provide returns that outpace it. Here's a look at how a climbing inflation rate could impact various investment types and asset classes.

- **Domestic Stocks** -- Although past performance is no guarantee of future returns, historically, stocks have provided the best potential for long-term returns that exceed inflation. An analysis of holding periods between 1926 and December 31, 2010, found that the annualized return for a portfolio composed exclusively of stocks in Standard & Poor's Composite Index of 500 Stocks was 9.93% -- well above the average inflation rate of 3.01% for the same period. However, over shorter time periods the results are not as appealing. For the 10 years ended December 31, 2010, the S&P 500 returned an average of only 1.41%, compared to an average inflation rate of 2.33%.<sup>3</sup>
- **International Stocks** -- Diversifying into foreign markets may help provide downside protection when the U.S. economy sputters.<sup>4</sup> During the same 10-year span that ended December 31, 2010, the Morgan Stanley Capital International (MSCI) EAFE, which is comprised of established economies such

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as Germany and Japan, outpaced U.S. inflation with an average return of 3.94%. The MSCI Emerging Markets index, which tracks developing world economies such as Brazil and China, was even more stellar, returning an average of 16.23%.<sup>5</sup>

- **Bonds** -- Historically, investors have turned to shorter-term corporate and high-yield bonds for protection in rising-rate environments.<sup>6</sup> There are two types of bonds that receive a lot of investor interest when inflation starts to rise: Treasury Inflation-Protected Securities (TIPS) and I Savings Bonds. Both TIPS and I bonds are types of fixed-interest rate bonds whose value rises as inflation rates rise.
- **CDs and Other Cash Instruments** -- The Federal Reserve is still keeping a tight lid on interest rates, forcing investors who hope to keep pace with inflation by investing in cash instruments facing a harsh reality. The rates on a 1-year CD are averaging under 1%, while a 5-year CD is yielding just over 2%, according to Bankrate.com. Money market and other bank savings accounts are also averaging well under 1%.

Although many economists project overall U.S. inflation to remain modest in the near future, most see an uptick down the road. For investors, a well-rounded portfolio may be your best weapon. The key is to consider your time frame, your anticipated income needs, and how much volatility you are willing to accept, and then construct a portfolio with the mix investments with which you are comfortable. Consult your financial professional to discuss your specific needs and options.

<sup>1</sup>Source: U.S. Bureau of Labor Statistics, June 2011.

<sup>2</sup>Sources: TradingEconomics.com and U.S. Bureau of Labor Statistics, June 2011.

<sup>3</sup>Sources: Standard & Poor's, U.S. Bureau of Labor Statistics. The S&P 500 is an unmanaged index. It is not possible to invest directly in an index. Past performance is no guarantee of future results.

<sup>4</sup>Diversification does not ensure a profit or protect against a loss in a declining market.

<sup>5</sup>Source: Morgan Stanley. The MSCI EAFE and MSCI EM are unmanaged indexes. It is not possible to invest directly in an index. Past performance is no guarantee of future results.

<sup>6</sup>Bonds are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rates rise and are subject to availability and change in price.

## Calculating Your Retirement Needs

Calculating a retirement savings goal is one of the most important steps investors can take to help determine if they are on pace to meet that goal. However, less than half of American workers have tried to figure out how much money they will need to accumulate for retirement;<sup>1</sup> and the wide majority of these individuals admit that they either guessed or did their own calculations. What about you?

### Planning Matters

What's important to realize is that the exercise of calculating a retirement savings goal does more than simply provide you with a dollars and cents estimate of how much you'll need for the future. It also requires you to visualize the specific details of your retirement dreams and to assess whether your current financial plans are realistic, comprehensive, and up-to-date.

### Action Plans

The following four strategies will help you do a better job of identifying and pursuing your retirement savings goals.

1. **Double-check your assumptions.** Before you do anything else, answer these important questions: When do you plan to retire? How much money will you need each year? Where and when do you plan to get your retirement income? Are your investment expectations in line with the performance potential of the investments you own?
1. **Use a proper "calculator."** The best way to calculate your goal is by using one of the many interactive worksheets now available free of charge online and in print. Each type features questions about your financial situation as well as blank spaces for you to provide answers. An online version will perform the calculation automatically and respond almost instantly with an estimate of how much you may need for retirement and how much more you should try to save to pursue that goal. If you do the calculation on a paper worksheet, however, you might want to have a traditional calculator on hand to help with the math. Remember that your ultimate goal is to save as much money as possible for retirement regardless of what any calculator might suggest.
1. **Contribute more.** Do you think you could manage to save another \$10 or \$20 extra each pay period? If so, here's some motivation to actually do it: Contributing an extra \$20 each week to your plan could provide you with an additional \$130,237 after 30 years, assuming 8% annual investment returns.<sup>2</sup> At the very least, you should try to contribute at least enough to receive the full amount of your employer's matching contribution (if offered). It's also a good idea to increase contributions annually, such as after a pay raise.
1. **Meet with an advisor.** A financial professional can help you determine a strategy -- and help you stick to it.

Retirement will likely be one of the biggest expenses in your life, so it's important to maintain an accurate price estimate and financial plan. Make it a priority to calculate your savings goal at least once a year.

<sup>1</sup>Source: *Employee Benefit Research Institute, 2011 Retirement Confidence Survey, March 2011.*

<sup>2</sup>This example is hypothetical and for illustrative purposes only. Your results will vary. Investment returns cannot be guaranteed.

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