# PRIVATE BANKING UPDATE

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## Is Increased Inflation on the Horizon?

Here is some information you may find interesting.

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

Recently, worries about inflation have been stoked by a dropoff in quantitative easing by the Federal Reserve, largely due to an improving economy. With a strenthening economy and soaring federal deficits, many experts feel that prices in the United States will inevitably pick up their pace.

### Inflation Rates Around the World, 2013[1]

| Country | Rate |
|---|---|
| Brazil | 6.3% |
| Canada | 1.1% |
| China | 2.7% |
| France | 1.0% |
| Germany | 1.6% |
| Greece | -0.8% |
| India | 10.9% |
| Italy | 1.6% |
| Japan | 0.0% |
| Mexico | 3.6% |
| Russia | 6.7% |
| United Kingdom | 2.7% |
| United States | 1.4% |
| Venezuela | 37.9% |

### 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, 2013, found that the annualized return for a portfolio composed exclusively of stocks in Standard & Poor's Composite Index of 500 Stocks was 9.90% -- well above the average inflation rate of 2.98% for the same period. However, that can vary over shorter time periods. For the 10 years ended December 31, 2013, the S&P 500 returned an average of 7.40%, compared with an inflation rate of 2.37%.[2]
- **International Stocks --** During the same 10-year span that ended December 31, 2013, the Morgan Stanley Capital International (MSCI) EAFE, which is composed of established economies such as Germany and Japan, outpaced U.S. inflation with an average return of 7.39%. The MSCI Emerging Markets index, which tracks developing world economies such as Brazil and China, was even more stellar, returning an average of 10.53%.[3]
- **Bonds --** Historically, investors have turned to shorter-term corporate and high-yield bonds for protection in rising-rate environments.[4] 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 one-year CD are averaging under 1%, while

a five-year CD is yielding an average of under 2%, according to *Bankrate.com*. Money market and other bank savings accounts are also averaging well under 1%.[5]

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.

[1]*Sources: International Monetary Fund, World Economic Database, October 2013. Some value are estimates. For the 2013 calendar year.*

[2]Sources: Standard & Poor's; U.S. Bureau of Labor Statistics. The S&P 500 is a unmanaged index. It is not possible to invest directly in an index. Past performance is no guarantee of future results.

[3]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.

[4]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.

[5]Source: *Bankrate.com*, June 14, 2013.