# How inflation can impact your investments and your wallet

It's impossible to turn on the news these days without seeing something about rising prices—whether it's for food, gas, or other day-to-day goods. Indeed, inflation—the term economists use when talking about year-over-year price increases in goods and services—jumped by 5.7% in Canada for February, the highest annual gain since August 1991. A confluence of factors can be attributed to the rise, including: surging demand as people begin to return to pre-pandemic life, continuing supply chain issues, and geopolitical unrest.

Given how rare this kind of inflation increase has been over the last 30 years, many Canadian investors have little experience dealing with increasing costs. So, if you're troubled by these soaring price tags, you're not alone. The big question then becomes: how does climbing inflation impact your wallet and your investments?

In the aggregate, inflation isn't great news. First, you may find yourself spending more on many day-to-day items, including food, fuel, furniture, and clothing to name a few. If your spending increases that means you could have less money to save. You may need to adjust your budget to ensure you're covering your costs and leaving some money left over to invest.

Inflation also increases your cost of living in retirement for whatever future items or goals you're saving for. For instance, say you've been trying to get your portfolio to $1 million by the time you turn 65. Now, your retirement might cost $1.3 million. To achieve that long term goal, you'll either need to save more money or start thinking about economizing aspects of your retirement lifestyle.

Inflation also negatively affects the current value of a broad swath of assets found in a typical investment portfolio. These can include:

- Cash – if you are not earning anything on it, you are actually losing in real, after-inflation terms
- Bonds – especially those with distant maturity dates
- Stocks of companies in highly regulated industries that can't readily increase their prices to match rising costs
- Stocks of companies with no sustainable competitive advantages that cannot pass through to customers the higher costs they are facing
- Stocks of companies with higher proportions of expected future cash flows (duration)—inflation devalues those future earnings in today's dollars

### What can you do about it?

While this may seem disconcerting, it's important to remember that even though you can't control inflation or how central banks try to offset its effects (like by raising interest rates), there are a few things you can do to effectively manage your finances and stress.

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### 1. Review your portfolio with a financial advisor

If you're feeling concerned that the world could be living with higher inflation for an extended period of time, you may want to talk to an advisor about potentially making some changes to your investments. Most importantly, you need to ensure you're well diversified, so that if one area of the market gets negatively impacted by inflation, others will hopefully continue to do well. While diversification is key to any portfolio, now's a good time to double-check that your funds hold a broad array of assets.

### 2. Keep in mind that the future is uncertain

Though inflation is constantly being discussed in the news, that doesn't necessarily mean higher-than-expected inflation will continue over the long term. Many other different scenarios may unfold, and your portfolio needs to be prepared for those potential outcomes as well, which is why diversification is so important. It's a good idea to avoid trying to predict what might happen (as no one really knows) and making a big change to your portfolio in response, which could potentially knock you off course from your long-term plan.

### 3. Be disciplined

Increased market volatility is another effect of inflation, which can be difficult to watch when checking your investments. That can lead to yet another big risk, this time behavioural: the desire to impulsively buy or sell something at the wrong time.

When it comes down to it, the most important thing investors can do is review their investing plan, and if it still reflects their goals and risk tolerances, recommit and have the discipline not to waver from it. Keep regularly contributing to your investment accounts, and if it makes sense, potentially increase those installments to ensure you are continuing towards achieving your financial goals. In other words, don't put undue pressure on your portfolio, and continue to pay yourself first.



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