Three Approaches to Adding Inflation-Hedging Assets

A mix of inflation-fighting assets is preferred because no single inflation-hedging asset outperforms in all inflation environments. Here are three ways to help fight inflation in your portfolio.

1. Diversified Portfolio Approach
   - **For investors who...** Need to diversify their portfolio AND want to hedge against inflation risk.
   - **Investment solutions** Asset allocation portfolios combine a mix of asset classes (including stock, bond and money market funds) with the objective to provide broad diversification in a single mutual fund. Most asset allocation portfolios include several underlying investments that are designed to help hedge against inflation risk. Additionally, portfolio managers monitor and rebalance the allocation of the underlying funds regularly.
   - **Implement the approach** Asset Allocation Portfolio Solution: In this example, an investor could purchase (or exchange existing holdings into) an asset allocation portfolio. The portfolio includes built-in allocations that are commonly used as inflation-hedging assets. The percent allocated to inflation assets will vary based on the portfolio chosen.

2. Comprehensive Inflation Approach
   - **For investors who...** Already have a diversified portfolio and want to add a single fund with the goal of hedging against a variety of inflation types and cycles.
   - **Investment solutions** A single, comprehensive mutual fund combines multiple inflation-hedging assets with the goal to provide a hedge during all periods of inflation cycles. Portfolio managers monitor and adjust the allocation of the fund's assets based on the changing inflation environment.
   - **Implement the approach** Inflation-Hedging Single-Fund Solution: Here, an investor with a hypothetical balanced portfolio (e.g., 60% stock funds, 40% bond funds) could allocate 10% of the portfolio—6% from stock funds and 4% from bond funds—into the single-fund solution. Remember, the actual allocation to inflation hedges will depend on the investor's unique situation.

3. Individual Funds Approach
   - **For investors who...** Already have a diversified portfolio and want to add a mix of individual stock and bond funds which are commonly used as inflation hedges.
   - **Investment solutions** Individual inflation-hedging bond and stock funds may include:
     - Inflation-linked bond funds (which may hold TIPS)
     - Real estate (REIT) funds
     - Commodities funds, which may hold producers of precious metals or natural resource-related products
   - **Implement the approach** Inflation-Linked Individual Funds Solution: In this example, an investor with the same hypothetical balanced portfolio (e.g., 60% stock funds, 40% bond funds) could allocate 10% of the portfolio—6% from stock funds and 4% from bond funds—into individual inflation-hedging stock and bond funds. Again, the allocation to inflation hedges will depend on the investor's unique situation.

Stock holdings may provide additional inflation-hedging exposure. Stocks of commodities producers and non-U.S. dollar denominated holdings in international funds are indirect inflation hedges in a portfolio.
Treasury Inflation-Protected Securities (TIPS): TIPS are a special type of U.S. Treasury security designed to address a fundamental, long-standing fixed-income market issue—that the fixed interest payments and principal values at maturity of most fixed-income securities don’t adjust for inflation. TIPS interest payments and principal values do. The adjustments include upward or downward changes to both principal and coupon interest based on inflation.

Real estate investment trusts (REITs) are companies, usually traded publicly, that manages a portfolio of real estate to earn profits for shareholders. Patterned after investment companies, REITs make investments in a diverse array of real estate such as shopping centers, medical facilities, nursing homes, office buildings, and apartments.

Commodities are bulk goods such as grains, metals and foods traded on an exchange or spot market (in which goods are sold for cash and delivered immediately).

Non-dollar investments—in the context of an inflation-hedging strategy—are assets with values that can move independently, and, ideally, in a non-correlated manner, from the value of the U.S. dollar. These are assets that have potential to serve as portfolio diversifiers away from the dollar when the dollar is expected to lose value in relation to other currencies. Non-dollar investments, in this context, can include foreign bonds, foreign currencies, foreign stocks, real estate, and commodities.

This information is not intended to serve as investment advice; it is for educational purposes only.

Diversification does not ensure a profit or protect against a loss in a declining market.

Rebalancing allows you to keep your asset allocation in line with your goals. It does not guarantee investment returns and does not eliminate risk.

Generally, as interest rates rise, bond prices fall.