Introduction

Inflation is defined as a sustained increase in the general level of prices for goods and services. We measure it as an annual percentage increase. As inflation rises, every dollar you own buys a smaller percentage of a good or service (IEA,1972). The Fed tries to sustain an inflation rate of between 0-3%.

Inflation affects different people in various ways. The impact inflation has on your portfolio depends on the type of investment you hold. There is now a widely-shared consensus, that high inflation does substantial damage to the economy, that moderate inflation does rather less damage, and that low inflation or price stability enables economies to work most effectively. With an open economy and low inflation bedded-in, it is necessary for investors to pay attention to real return from any investment, not nominal return (Alexander, Sharpe &Bailey, 2001).

1.my own home

All investments have some level of risk, even money in the bank. The risk here is that although you are highly unlikely to lose funds, your capital can over time, be eroded through inflation. Inflation risk will undermine the performance of your investment. Therefore, it is important to establish investment strategies in a low inflationary environment for real return.

Traditionally, investors believed that real estate is a good vehicle for hedging against inflation. Investing real estate would be one of the choice my own home considering. When buying property for the purposes of investing the most important thing you should always consider is the location. Unlike other investments, real estate is dramatically affected by the condition of the immediate area where the property is located, and other local factors (Cummings, 1993).

The other choice is that we could invest shares, because in a short term the rates of share returns are related to the rates of change in inflation. Although Share prices are affected by a number of forces, many of which are shifting constantly. For instance, inflation, prices on a single day can be affected by emotional reactions to news of change in interest rates, company profits, and so on. Share returns in a long duration are ahead of the rate of inflation. Looking at the impact of low inflation on Australian share returns, we could see that investing shares is still a good choice.

Figure 1 The impact of low inflation on Australian share returns

The impact of low inflation on Australian share returns

Australia (% pa)	1981-2001
Total return	13.6
• Dividends	4.6
• Capital growth	9.0
• Earnings	6.4
• change in valuations	2.6
Underlying return	11.0

Source: AMP Henderson, 2002

Furthermore, investing personal insurance is another component in our investment scheme. Those include income protection insurance, life insurance, medical insurance, property insurance. By that could protect future uncertainty and lose.

2.investment property

Real estate is regarded as a hedge against inflation, so investing in real estate in a low-inflation environment seems to be rational. Real estate investing doesn't just mean purchasing a house, it can include vacation homes, commercial properties, residential properties, land (both developed and undeveloped), condominiums,

along with many other possibilities. People, in general, are not stupid. They make rational decisions. Many have made a rational decision to invest in houses. The decision is rational for two reasons (Cummings, 1993)

First, over the last 30 years the return on housing investment has been above inflation. Over the 1990s, annual inflation has been kept stablely within a 0-2% range. At the same time, property prices have doubled (Baum,1991). Land is a scarce resource. There is a fixed supply of it. As population increases, demand for certain types of land increases and, in the absence of further supply, prices must and do increase. Land prices may rise and fall in the short term, but over the long term they will tend to rise faster than inflation. The supply of other goods, services and assets is generally not fixed. So as demand increases, supply also increases, limiting price increases.

The second reason investment in housing is rational is New Zealand's treatment of capital gains. Capital gains are not taxed in this country. On the other hand, interest income, company profits and wages and salaries are taxed. Assuming a tax rate of 33%, those obtaining their incomes from capital gains are 50% better off, after tax, than their counterparts who derive their earnings from taxable sources (Booth,1998,p23).

Currently it is not too difficult to invest in a commercial property venture that yields between 10 and 11 percent, without the burden of managing the building (Morgan, 1997,p48). Such high yields encourage investors to use commercial property as an income generator, when it is really a hybrid asset class that can produce growth and income.

3.interest-bearing investment

The real returns on interest-bearing investments are increasing in a low inflationary

environment. Income investors can get good returns while preserving their capital by investing in Treasury, municipal, corporate bonds, or in some derivatives like future and option (Sheet, 1994, p62).

Historically, interest-bearing investors have been lucky to get yields from interest income more than two percentage points above the rate of inflation. Treasury securities are a great choice these days, too. Yields are within a whisper of those on corporate bonds, which lack many of the advantages you get from Treasuries. Interest is exempt from state and local (but not federal) taxes. Payment of principal is assured upon maturity, and the bonds can easily be sold in the open market before maturity (Groeneveld, 1998).

Returns are often advertised or reported as a gross return and appear higher because they do not allow for tax and the effect of inflation. The hardest hit from inflation falls on the fixed-income investors. Suppose one year ago you invested $1,000 in a T-bill that yielded 10%. You are about to collect the $1,100 owed to you. Is your $100 (10%) return real? Of course not! Assuming inflation was positive for the year, your purchasing power has fallen and thus so has your real return. We have to take into account the chunk inflation has taken out of your return. If inflation was 4%, then your return is really 6% (Hing,2002,p13).

4.shares

According to the classical theory, the 'real value of unlevered equity will be invariant to inflationary or deflationary changes in the general price level so that in principle its current money value will rise in proportion to rates of inflation' (Lintner, 1975,p.268 cited in Sarnat,1978,p.19). In short term share returns are relatively high when inflation is relatively high, and relatively low when inflation is relatively low. The reason is that shares represent claims on real assets that should increase in value with inflation.

It is reasonable to assume that investors are more concerned with real returns than with nominal returns because real return reflects how much better off they are in terms of the purchasing power of their wealth. According, real returns of shares need to be analyzed. It is very tough to predict market movements. The long-term average return for Australian shares is 12.7% annually (as mentioned earlier), however it might not be reasonable to expect this level of return moving forward. The 1990s were a great time for investing, mainly due to low inflation and low interest rates (Coote,1997,p53).

Investors who try to maneuver market volatility may also run straight into another problem. If they sell their shares and invest elsewhere, say in a safe investment like a bank account, inflation may well erode their returns -leaving them even further away from achieving their long-term financial goals.

5.collectibles

Collectibles can take a long time to increase in value, and they offer no assurance as to their value in the future. Furthermore collectibles offer no income like other investments do. The one of the biggest advantages is that most collectibles increase in value along with inflation. As in the 1970s in the USA, even a severe recession will have only a temporary effect on collectibles (Bamford, 2000). Therefore that is the reason why some investors tend to invest collectibles during inflation. Many collectibles offer reasonable protection from inflation. However, there are some risks in investing collectibles, firstly look at the following aspects.

Firstly, collectibles are not very liquid, they can often be hard to sell at a desirable price. collectibles can be bought just about anywhere. More popular places are flea markets, antique stores, auctions, collectible retailers, garage sales, and more recently, online exchanges such as eBay (Hogan,2002).

Secondly, the maturity for a collectible can also widely volatile. For fads such as Beanie Babies, the price of the collectible can reach its peak very quickly. Other items such as antiques can take several decades before appreciating in value.

Furthermore, the true value can often be difficult to determine. The value of the collectible can vary widely but for the most part is reliant on supply and demand for the asset (Hogan,2002).

To sum it up, investing collectibles is a good choice in a low inflationary environment, which could become actively following the level of inflation. Also with low inflation investors tend to get biggest return from different investments, so investing in collectibles or not and how much do you want to invest become an essential question that investors should ask themselves.

Conclusions

In conclusion, because inflation erodes value, an important feature of any investment is its ability to provide a return in excess of the rate of inflation. Everyone knows the old saying, ‘Don’t put all your eggs in one basket.’ The same principle applies to the way you invest. Diversification can allow you, over time, to offset losses in one sector with gains in another. For instance, choosing a range of investments within your portfolio. Additionally, looking at results without taking into account inflation is the nominal return. The value you should care about is the growth of your purchasing power, referred to as the real return.

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