



**>: How to Profit From Inflation**

*Wednesday, April 16, 2008 / Teeka Tiwari*

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- Why Blockbuster's offer for Circuit City boggles Teeka's mind
- His near-term outlook for oil
- Several alternative energy ETF plays

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\$113 oil - WOW! There is no sugar coating how spectacularly bad \$113 a barrel oil is for corporate earnings. The Producer Price Index, also known as the PPI, tracks inflation at the wholesale level. Recently, we saw huge jumps in the prices that businesses are paying for raw materials. Most companies will not be able to absorb these costs. They will have to be passed onto consumers at some point, and those price hikes will show up in the Consumer Price Index, also known as the CPI.

Inflation is here my friends. The government can ex out food and energy all they want. I don't need a PHD in economics to figure that out. A quick trip to the grocery store will tell me all I need to know. Inflation kills stock prices because it compresses corporate margins. If corporate margins are down, earnings are down and if earnings are down, stock prices are down.

Now don't misunderstand me. I am not suggesting that it's game over for the stock market - far from it. What I am saying is that it appears that we are stuck in what is essentially a sideways market. A market that is range bound. In 2000, the DOW hit 12,000. Eight years later it's at 12,300. The S&P 500 hit 1526 in 2000; it's now at 1,328.

In the interim we've had some terrific trading opportunities, but they were range bound plays. For eight years we have not experienced a net new meaningful rally in two indexes that 87% of all mutual fund money is tied to. In fact, if you have not been an adept sector player, your profit making opportunities have been slim indeed. The poor buy and hold S&P 500 index investor has been slaughtered over the last 8 years.

My point is that the game has changed. Anybody born from 1965 onward has never experienced the type of market that we currently find ourselves in. Think about that. That's an awful lot of dumb money running around managing your money!

Most professional money managers (I'm talking about the mutual fund guys here) have just not yet adapted to this market. These managers came from a 20 year run where all you had to do was index your way to billions in fees. Those days are done, finito. Maybe they will be back in another 8-12 years. But if you are using the DOW and S&P 500 indexing as a method to fund anything, you are fighting a war with bow arrows while everyone else has sub-machine guns.

You just can't win.

While the rest of the world scrapes through the investment tea leaves looking for the bottom in financial stocks the smart money has been quietly busy at work in many other areas of the market.

You must position your investments for where we are now, like the smart money is doing, not where we've been. Remember: 87% of all mutual fund assets are correlated to the S&P 500. That's a lot of mediocrity going on with your money.

You want to start looking for sectors that will do well regardless of inflation or general economic malaise. You want to be looking at food companies, oil and oil service stocks, fertilizer stocks, agriculture equipment makers, steel, precious metals, foreign currencies, utilities, and direct ownership in commodities. Corn, sugar, wheat, soy etc? If you don't have a strategy for gaining exposure to these sectors, your current wealth is going to be ravaged by inflation, and your future wealth could fail to materialize.

I know that we are conditioned to focus on the DOW and the S&P 500. I also know that if we get any type of a decent number from Citigroup, JP Morgan or Merrill this week we could have a very nice run in both indexes. That's great, but that's not where the real money is being made right now.

Right now you must start taking a long hard look at sectors like the food and beverage group and the utilities. These are two sectors that are just beginning to get ready to run. They also happen to be great safe haven areas in times of uncertainty, like now. During difficult economic times, these stocks can gun much higher.

ETFs are a great way to play this space if you are unsure which stocks to buy. However, be careful of the Utility ETFs. I've noticed a lot of poorly performing stocks are packed into them. This is one sector where you will probably be better served by individual stock ownership.

Some Food/Beverage ETFs that warrant your attention include

- ? iShares DJ US Consumer Non-Cyclical Sector **IKYK**
- ? Consumer Staples Select Sector SPDR Fund **XLP**
- ? PowerShares Dynamic Consumer Staples Sector **PSL**
- ? PowerShares FTSE RAFI Consumer Goods Sector **PRFG**
- ? Powershares Dynamic Food and Beverage **PBJ**
- ? Vanguard Consumer Staples ETF **VDC**
- ? Rydex S&P Equal Weight Consumer Staples **RHS**
- ? Market Vectors Agribusiness ETF **MOO**

As a general rule, if you are going the individual stock route you are going to want to focus on companies that sell internationally. These companies will receive a nice earnings boost when they translate their income from foreign currencies back into US Dollars. This is because, in all likelihood, the US Dollar will continue to trend lower.

I cannot imagine a scenario where I would want to own a mutual fund over an ETF. It just doesn't make sense. The fees of a mutual fund, coupled with their archaic trading nature, makes them awful investment vehicles. You want liquidity, you want the immediate ability to buy, sell, short, or trade options on any sector at anytime. The only investment vehicle I know of that allows you to do all of that without taking on individual company risk are ETFs.



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