

# Financial Focus

## Should Rising Oil Prices Affect Your Investment Strategies?

Every time you fill up your gas tank, you are painfully aware that oil prices are high—really high. And rising oil prices can affect the cost of many other goods and services, from food to airline tickets. So, as a consumer, you know the impact of an increase in the cost of oil, but how about as an investor? Should rising oil prices change the way you invest?

Before we look at this question, let's quickly review why oil prices have gone up so far and so fast. First, the price of oil is reflecting the law of supply and demand; the world's oil supply has stayed relatively tight recently, while demand has continued to rise. Second, oil is a commodity priced in dollars, so if the dollar falls in value—as has been the case lately—then the price of oil will rise.

Will these two factors continue to drive up the price of oil? It's hard to predict. However, as an investor, you do want to know how the current state of affairs—that is, elevated oil prices—will affect your investments. Specifically, in this environment, what market sectors will be influenced? And how?

Not surprisingly, the stocks of many energy companies tend to do well when prices are high. At the same time, the automobile and airline industries, and some elements of the retail sector, may be negatively affected.

Does this mean you should make some drastic changes to your investments? Not if you follow a strategy of buying and holding a diversified array of quality investments. (Keep in mind, though, that diversification, by itself, cannot guarantee a profit or protect against a loss in a declining market.) However, you may want to make some adjustments. For example, if the increased value of your energy stocks has caused your portfolio to become “overweighted” with these stocks, which can be volatile, you may want to consider some type of rebalancing.

But rather than focus on how rising oil prices can affect individual market sectors, try to look at the bigger picture. As mentioned earlier, rising oil prices can lead to higher overall inflation, and over the long term, inflation is a much more serious threat to your portfolio's health than a short-term spike in oil prices. Consider this: If inflation rises three percent a year, which has been the average increase over the past eight decades, then everything you buy today could cost twice as much in 24 years.

To protect yourself from the ravages of inflation, you need to own investments that offer the potential for rising income, such as quality dividend-paying stocks. By doing some research, you can find stocks that have paid (and increased) dividends for 20 to 25 consecutive years. (Be aware, though, that companies are not obligated to pay dividends, and can cut or discontinue them at any time.)

By making timely adjustments in response to events such as oil price “shocks,” and by following a long-term strategy of owning an appropriate array of quality investments, you can continue working toward your financial goals...now, and in the future.