Rising Inflation

Investors Need to Account for Rising Inflation

A good rule of thumb is to assume inflation will be at least 3% every year

All investors would be well served to understand the latest Consumer Price Index data from the Department of Labor. Because inflation will impact your long-term retirement strategies.

Inflation Matters

In simple terms, inflation is defined as an increase in the general level of prices for goods and services. Deflation, on the other hand, is defined as a decrease in the general level of prices for goods and services. It matters because inflation decreases the purchasing power of your money in the future. If inflation is say 10% (considered high by the way), then a loaf of bread that costs $1 this year will cost $1.10 the next year.

Inflation in the U.S. has averaged around 3.3% from 1914 until 2022 and it has averaged about 3.7% for the past 60 years. The annual inflation rate as of October 13, 2022 came in north of 8%, an annual rate not seen in over 40 years.

Watching Inflation

The U.S. Department of Labor Bureau of Labor Statistics publishes monthly measures of inflation when it calculates the Consumer Price Index.

On October 13th, it was reported that the Consumer Price Index for All Urban Consumers advanced 0.4% in September. But the 12-month inflation number came in at 8.2%.

The reasons for the large change were identified as follows:

- The food index is up 13.0% over the last year;
- The energy index increased 19.8% over the last year;
- Fuel oil is up 58.1% over the last year;
- New vehicles are up 9.4% over the last year; and
- Transportation services are up over 14.6% over the last year.

Accounting for 3% Inflation

The question for investors to think about is not whether inflation will find its way into the broad economy – it has. More importantly, what should an investor do about it?

While no simple answer covers every situation, generally speaking, your long-term retirement strategies should account for inflation. And a good rule of thumb is that you assume inflation to be at least 3% – its historical average.

If you’re wrong and we find that the inflation rate for the next 25 years turns out to be less than your assumed 3%, then the purchasing power of your retirement savings will be more, not less.

Your financial advisor can help model different retirement scenarios while accounting for inflation.

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