ADVISOR

Advisor Investing

Advertiser Disclosure

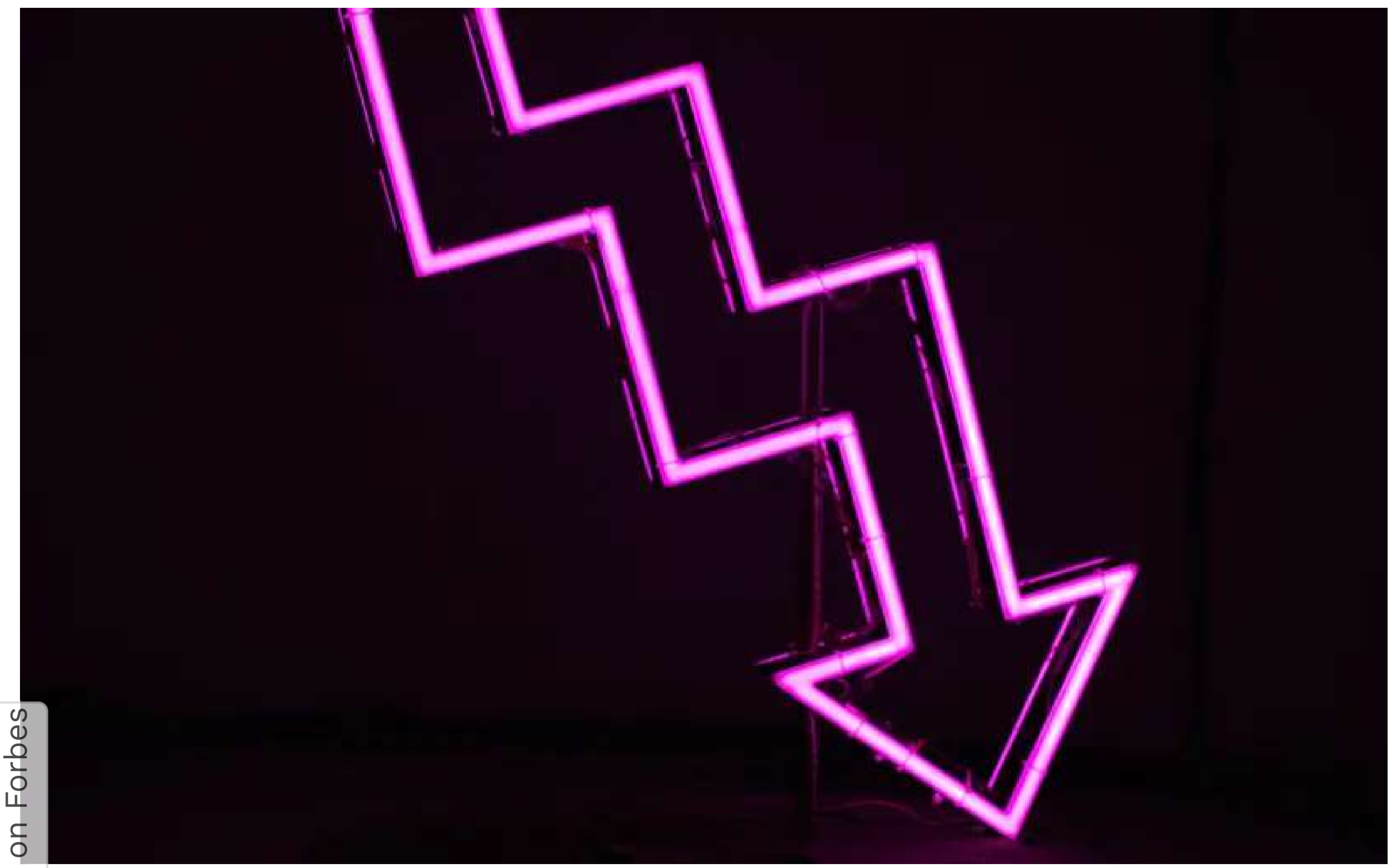
Inflation Outlook 2023

Andrew Michael
Editor

Kevin Pratt
Editor Reviewed By

Published: Apr 19, 2023, 9:20am

Editorial Note: Forbes Advisor may earn a commission on sales made from partner links on this page, but that doesn't affect our editors' opinions or evaluations. We offer information about investing and saving, but we do not offer any personal advice or recommendations. If you aren't sure whether investing is right for you, or which investments are right for you, please consult an authorised financial adviser.



Cookies on Forbes

Table of Contents

ADVISOR

While this is down from the 11.1% recorded in the year to October 2022 – a 41-year high – the figure remains painfully elevated.

The reason inflation is deep in double-figure territory is thanks to a toxic cocktail of economic conditions. These include the knock-on from soaring energy prices – triggered in large part by the war in Ukraine – coupled with rising interest rates and global supply chain bottlenecks.

Each of these factors has combined to produce a lengthy and worsening cost-of-living crisis for numerous households and businesses.

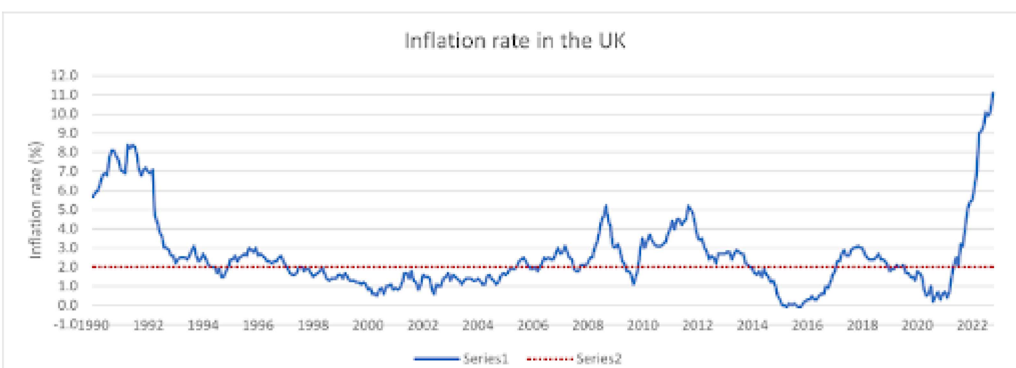
In recent years, prior to 2022, inflation had been relatively low. But, given the current state of play, it's only natural for people to be concerned about what lies ahead on the inflation front as we continue through 2023.

Here's a reminder of why inflation matters to our finances.

What is inflation?

Inflation is the term that's used to describe the increase in prices over time. The UK government sets an inflation target of 2% which the Bank of England is tasked with maintaining using monetary policies including the raising and lowering of interest rates via changes to the 'Bank Rate'.

Broadly speaking, inflation has remained relatively stable in the UK over the past 30 years as the following graph shows. The blue line in the chart represents the UK's actual inflation rate and how it has varied compared with the Bank of England's continual 2% target (red line).



Source: ONS

As the chart shows, inflation has soared over the past 18 months or so, rising from about 2% in 2021 to today's eye-watering double-digit figure of 10.1%.

Double-digit inflation has a devastating impact on the real value of cash at a time when the best easy-access individual savings accounts are only paying around 3% and about a percentage point higher for the best high interest savings accounts.

What's the outlook for inflation?

Forecasters agree that inflation will start to come down in 2023 and the Chancellor of the Exchequer, Jeremy Hunt, is aiming to halve the inflation figure by the year-end. More generally, however, there is less consensus about the size and shape of the retreat.

Samuel Tombs, chief UK economist at Pantheon Macroeconomics, says: "Looking ahead the headline rate of CPI inflation will likely drop to about 8.0% in April, as energy's contribution falls on the anniversary of surges in electricity, natural gas and motor fuel prices."

"The recent slowing of food producer output prices and farm gate prices should mean that food CPI inflation falls sharply over the next six months too."

and food and services inflation is proving troublesome. There is a growing suspicion the UK's inflation is of the stickier variety, and there is much more work for the Bank to do. It means the job of reining in price rises without inflicting collateral damage on the economy looks increasingly tricky to pull off."

Marcus Brookes, chief investment officer at Quilter Investors, says: "For as long as the economy can hold up, the Bank of England will keep the option of interest rate rises firmly on the table."

"With the headline rate of inflation eventually coming down to hopefully more palatable levels, there will be an increased focus on what is going on under the bonnet with core inflation. This measure failed to shift in March and this will be a real concern to the BoE. Should that fail to fall meaningfully in the next couple of months, then more aggressive monetary policy from the BoE may be required yet again."

What can investors do about inflation?

Investing is one option for savers looking to keep their money in line with – or beat – inflation. But this is a far from risk-free option, with the potential for loss of capital along the way.

David Henry, investment manager at Quilter Cheviot, says that, during periods of rising inflation, real assets such as stocks and shares, property and commodities, tend to perform better than cash or bonds: "In sterling terms, we looked at the performance of both UK and international stocks during periods of rising inflation since 1970 and found that UK markets tended to outperform global peers during these periods.

"This is most likely due to the UK market's longstanding relatively high exposure to energy and commodity sectors. An obvious 'hedge' to the current cost of living crisis would be to hold shares in an energy producer."

Charles Stanley's Rob Morgan says: "Protecting against high inflation is difficult for investors. Higher inflation, and higher interest rates to curb it, has an adverse effect on most asset prices.

"The problematic scenario for investors is that a simplistic traditional portfolio of equities and conventional bonds is not inflation resilient."

But he says there are a small number of areas that can help diversify a portfolio while helping to counter the effects of inflation. These include:

Infrastructure assets which often generate revenues that are contractually linked to inflation rates.

Index-linked bonds that pay an income, a component of which is inflation-linked.

Gold which sometimes does well in inflationary times, especially where interest rates do not rise sufficiently to compensate for stubborn inflation.

As with any investment, these assets become commensurately more expensive if lots of investors have the idea of protecting their portfolios at the same time.

Investing Guides

Guide To Investing

Best Index Tracker Funds 2023

Best Investment Trading Apps 2023