

FACT SHEET
The Effect of Inflation

The real spending power of money deteriorates over the years as a result of inflation. This is demonstrated by the following table which shows the effect of inflation on a notional investment of £1,000.

Inflation Rate (% pa)	Real Value 5 years £	Real Value 10 years £	Real Value 15 years £	Real Value 20 years £	Real Value 25 years £
2	905	820	743	673	609
3	862	744	642	554	478
4	822	676	555	456	375
5	783	614	481	377	295
6	747	558	417	312	233
7	713	508	362	258	184
8	680	463	315	215	146
9	650	422	275	178	116
10	621	386	239	148	92

For the first time in two years, the rate of inflation as measured by RPI, fell below the target of 2% and is likely to remain below target at least in the short term with the potential threat of deflation. However, the RPI, Retail Price Index and CPI, Consumer Price Index, no longer accurately reflect the impact of real inflation. Looking to the medium term, future governments may welcome, even encourage, a dose of inflation to mitigate the impact of record government debt. The IMF, International Monetary Fund, have warned Gordon Brown the Government must introduce a credible plan to reverse the rapid deterioration of the public finances.

If real inflation rises there is a danger that the rate of inflation will be higher than the rate of return from cash on deposit. This is a reversal of the position between 1995 and 2008 when interest rates net of income tax outperformed inflation. This was an exceptional period that is not likely to be repeated.

Whilst in theory, cash on deposit would appear to be a low risk investment, in reality there is a material risk of the value falling in real terms. An investor can seek to protect against inflation by investing in the following asset classes:-

- Quoted Shares – ideally non-cyclical companies such as the utilities who are not over borrowed and are able to maintain a dividend.
- Well let Commercial Property either directly or through a Collective Fund such as an authorised unit or investment trust.
- Index Linked National Savings Certificates.
- Index Linked Government Gilts.
- Investment Grade Corporate Bonds.

Forrester-Hyde Ltd
 Authorised and Regulated by the Financial Services Authority
 19 Clifftown Road, Southend-on-Sea, Essex SS1 1AB
 Tel: 01702 432532 – Fax: 01702 431466
 Email: Postmaster@forrester-hyde.co.uk
 Web: www.forrester-hyde.co.uk