MANAGING INFLATION IN RETIREMENT

alphastar
WEALTH MANAGEMENT
Emerald Coast

INTRODUCTION

Last year, there were some notable occurrences in the market, including a decline in the overall stock market, a hot job market that may show signs of cooling down, rising prices, and the Fed taking aggressive steps to control inflation. You may have noticed that the things you buy regularly have become more costly, and you may be pondering if inflation will stay high. For individuals close to retirement or already retired, it is essential to take measures to protect themselves from the eroding effects of inflation. As your first step to understanding your options, this guide will cover the following topics:

1. **A History of Inflation's Effects**
2. **Inflation and the Federal Reserve in Today's World**
3. **A Few Options for Inflation Management**

A History of Inflation's Effects

During the 1970s, Americans experienced inflation at more than 10%, resulting in considerable cost increases. While inflation rates have been relatively low for the past 13 years, there is an ensuing resurgence of inflation, and there's no telling how long it could last or if it will bounce back after it subsides.[1]

The Senior Citizens League calculated that the purchasing capacity of the average Social Security benefit decreased by one-third since the year 2000 due to insufficient increases in benefits that can't match the inflationary prices of drugs, food, and housing.[2] Even though Cost of Living Adjustments (COLAs) change yearly to compensate for inflation, they don't fully offset the rising costs.

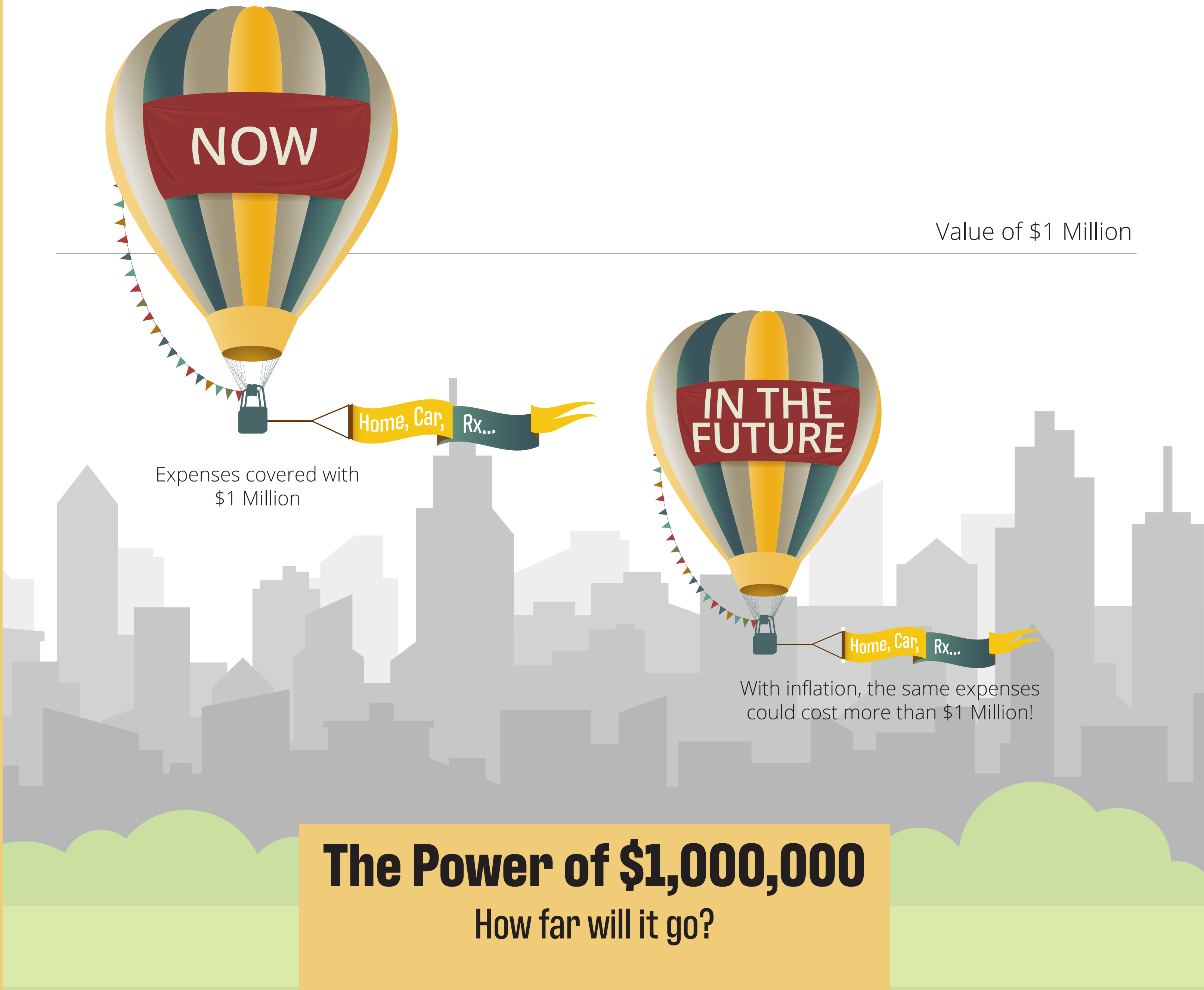
In 2022, the 8.7% cost-of-living (COLA) adjustment attempts to compensate for resurgent inflation. In past years, the adjustment wasn't very high. In 2021, the COLA was only 1.3%, and there were years when it was as low as 0.3% (2016) and 0% (2015).[3] Although this year's COLA is high, there is no guarantee that there will be more to come. It is crucial to consider the long-term effects of inflation on your Social Security benefits and your other sources of income and savings for retirement.

Take a look at overall prices from 1960 to 1980 and today:

	1960	1980	2022
A Dozen Eggs	57 cents[4]	84 cents[8]	$4.25[12]
Gallon of Milk	36 cents[5]	$1.12[9]	$4.21[13]
Median Home Price	$19,256[6]	$55,392[10]	$380,279[14]
Buying Power of $100	$100[7]	$40.08[11]	$10.38[15]

How Will Inflation Affect You?

In essence, inflation reduces the value of each dollar. In June of 2022, inflation was 9.1%, the highest in 40 years.[16] To illustrate the effects of inflation, 7% for 10 years, $1 million would be worth around $508,350. If there were 2% inflation for 20 years $1,000,000 would only be able to buy $672,971. When planning for retirement, think of the cumulative effect of inflation on your savings as it could last longer than 20 years.

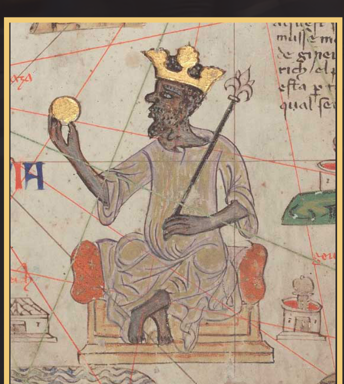


Inflation in Today's World

There are a few triggers for inflation, such as increased government spending in response to the COVID-19 pandemic, and the cuts in international oil production which have caused fuel prices to soar. These are just a few of the triggers that have caused a rise in the cost of goods and services. These are just a few of the triggers that have caused a rise in the cost of goods and services. Furthermore, supply chain disruptions add to inflation by causing product shortages. To counteract these effects, the Federal Reserve has increased interest rates, which leads to a contraction of the economy and quells inflation, though it carries the risk of causing a recession.[17,18]

The action by the Federal Reserve, as well as the ending of COVID economic relief programs, have slowed the growth of the US economy. As the purchasing power of the typical household continues to erode, the decrease in demand may lead to higher unemployment, decreased wages, and less household spending. All these factors tend to cause uncertainty in the stock market. As a result, retirees who depend on their savings and investments feel the impact.[19]

FUN FACT:



Mansa Musa depicted holding a gold coin from the 1375 Catalan Atlas. (Public Domain)

We've touched on inflation in the US as it pertains to the current economic climate... But inflation is an ancient concept!

The ancient Malian King, Mansa Musa, the richest man ever to walk the earth, caused massive inflation when he traveled from Mali to Egypt in 1324 on a trip to Mecca, where along the way he poured golden goods into commoners pockets. It took 12 years for the Egyptian economy to recover, and the event of Musa's wealth reached as far as Europe.

https://www.ancient-origins.net/weird-facts/mansa-musa-egypt-0017070

A few options for Inflation Management

It is likely that this period of recession and inflation will not be the only difficulty you will encounter during your retirement. Even though current interest rates are increasing, retirees are not likely to make significant returns by just keeping their funds in a bank account or a Certificate of Deposit. Meanwhile, a turbulent stock market may cause many people to become apprehensive about investing their retirement savings.

Our objective is to assist you in finding a middle ground and devising an investment strategy that is compatible with your risk tolerance. A strategy could involve combining stocks and bonds, rebalancing your portfolio, investing in inflation-protected annuities, and exploring other possibilities.

What is an Inflation-Protected Bond?

There are a couple of different types of inflation-protected securities. Treasury Inflation-Protected Securities, or TIPS for short, are bonds that can be bought and sold on secondary securities markets. For example, you can buy and sell TIPS the way you can buy and sell stock through your in-person or online broker. Thus, you may find exposure to TIPS in your investing accounts. TIPS offer an interest yield based on the rate of inflation as dictated by the rate of change of the Consumer Price Index. If inflation rises, the TIPS will rise commensurately. However, principal can decrease with deflation.[20]

Series 1 Savings Bonds, or I Bonds, are a little different. I Bonds have a similar structure for their interest calculation, however, you can purchase them directly from the Treasury online using TrasuryDirect.gov, and via paper purchase using your tax refund. In addition, you are only allowed up to $10,000 electronically and $5,000 using a tax refund for a total of $15,000 worth of I Bonds per year. I bonds last 30 years where, at expiry, you are paid back your principal. In the periods leading up to expiry, you are paid a combination of a fixed annual interest rate defined at the time of purchase, and a variable semiannual inflation rate.[21]

Alternative Assets

Gold and precious metals are a common go-to for those looking to protect against inflation. Many credit gold with having an intrinsic value that has lasted millennia. For this reason, gold is often purchased during times of turbulence in hopes of insulating their wealth from any institutional or national shake-up. While gold can be a great option for some people, there is no telling the future performance of an asset class, even gold or precious metals. Making an emotional decision to invest in an unpredictable asset class can introduce new risks when added to your portfolio. A financial professional can work with you to determine how to structure your portfolio to suit you.

Inflation Protection with Annuities

Series 1 Savings Bonds can help safeguard against inflation, but the maximum amount you can buy annually is $15,000.[22] On the other hand, there is no restriction on how much you can invest in an inflation-protected annuity (IPA). An IPA offers a real rate of return that is equivalent to or surpasses inflation.[23]

Fundamentally, an annuity is a financial product that receives a lump-sum premium and pays out installments over the insured's lifetime. An annuity is designed to make sure you don't outlive your finances by providing regular payments for the rest of your life, and can help protect against the hardship on your family of your permature death. Deferred annuities have an accumulation period in which the principal can gain interest before payments commence. Numerous annuity options are available, and our experts can work with you to determine how they can protect and augment the money you've earned.

A Financial Professional is Your Guide

The right strategies depend on your unique situation, market risk tolerance, and income needs. There's no single answer for how to beat inflation, but we can help you create a strategy to help protect what you've earned and generate a reliable income in retirement.

Reach out to us today to get clarity on your inflation management options.

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Disclosure

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[Graph data presented is dynamically displayed. Adjust dates for desired time periods.]

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[NOTE: Data is presented as of January 2023 and is subject to change]

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