

Inflation – Up, Up and Away?

For most of us the rate of inflation is considerably above the 3% claimed by the Government. It seems to me that the only items that seem to cost less each year are electrical goods and possibly clothing, with almost all other forms of expenses increasing at what seems like a rate way above 3%. The rising price of a barrel of oil has obvious knock-on effects on anything that needs energy. I recently came across a good website called www.petrolprices.com where you can register for free to receive weekly emails about the cheapest petrol in your area. I suggest you have a look and hopefully benefit from reducing your outgoings on fuel, of which a significant proportion of the cost is actually tax.



Inflation will erode spending power over time. Consider that a 3% rate of annual inflation will roughly halve the value of your money over 25 years. Turning this on its head, let's say you want to have an income of £40,000 in your retirement in 25 years time. This would need a pension fund of roughly £800,000 in today's money; however, if inflation runs at 3% each year then the fund really needs to be £1.6m – which happens to be only £5,000 shy of the current lifetime allowance for pensions.

The value of £100 over time against differing rates of inflation

Inflation	10 years	15 years	20 years	25 years	30 years	35 years
2%	£82	£74	£67	£60	£55	£49
3%	£74	£63	£54	£47	£40	£34
4%	£66	£54	£44	£36	£29	£24
5%	£60	£46	£36	£28	£21	£17

The time-frames may seem large, but we will all recall items from our childhood that were once much cheaper than they are now. Extrapolate this forward - you are entering retirement, you are healthy and might expect to live a further 25 years?

It is partly for this reason that we tend to suggest investing a percentage of your income rather than a fixed amount, that way at least any salary inflation is covered to some extent. I know it sounds like a lot, but in reality you need to be saving at least 10% of your salary towards your retirement. The sensible thing to do is to pay this each month by direct debit, or from your payslip, that way you do not "miss" the 10% and are forced to live within 90% of your income. This is what is sometimes referred to as "paying yourself first" – setting aside payment for your future, rather than paying everyone else first and then being nervous about committing the little you have left for your own future well-being. It has got to be first. It has got to be automatic. Your budget ought to come *after* you have allocated money for your future, not before.

If you did not appreciate it already, this is why Governments believe that inflation must be controlled. This is done primarily by trying to reduce expenditure – which is achieved by raising interest rates (encouraging saving rather than borrowing) and taxation – reducing available money to spend.

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