FINANCE UPDATES
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Hampshire Hill
Independent Financial Advisers

BEAT INFLATION THROUGH SAVVY INVESTMENTS

Inflation may hit 7% this spring; investing can help.

Soaring inflation is about to affect everything we do this year and preparing now may be the best way to head off that threat.

Last month, Ofgem raised its energy prices cap by 54% – bad news for homes that are not on fixed deals with their supplier.

From 1 April 2022, this will cause default bills in the average household in England, Scotland, and Wales to increase to £1,971 – up from £1,277.

Investments are a good option to hedge against rapid inflation, as the value of the assets you buy can increase in real value.

However, while taking on this additional risk with your savings can provide returns that outstrip rising costs, you could also lose money as well.

But, when everyone's buying power is falling, it's vital to arrange the right kind of investments to try and beat inflation.

Central to that is the allocation process of dividing your investments between different assets, such as cash, bonds, shares, and property.

This helps to spread risk through diversifying your investment portfolio – in other words, by not putting all of your eggs in one basket.

We can help you develop an investment strategy which will factor in inflation – and use it to help build your wealth, not erode it.

WHAT CAN YOU INVEST IN?

You can invest in almost anything nowadays, but the most popular options in the UK are shares, funds, bonds, gilts (government bonds), and property.

Investing in shares typically involves putting your cash into the stock market, usually by purchasing company stock or via funds.

With funds, you pool your money with other people's investments and leave the decision-making to a fund manager, who chooses shares on behalf of the fund's investors.

Bonds and gilts are fixed-income investments that generally offer less risk than investing in shares and funds. Corporate bonds are portions of loans made to companies, while government bonds are loans made to governments. UK Government bonds are known as gilts.

Property remains a popular long-term investment strategy, especially with low interest rates resulting in lenders offering some generous mortgage offers.

However, high house prices in the UK and changes to tax legislation in recent years mean this form of investing offers less returns than in its heyday.

UNDERSTANDING RISK

We invest to try and make money, not lose it. But the problem is that investing inevitably means risk. The risk is usually not that your investment will lose all its value, although that can happen. The risk can be expressed as volatility.

As a general rule of thumb, the higher the potential returns, the higher the volatility. This means the investment which could make you a great deal of money in a short time carries a bigger risk of losing at least some of it.

When we assess your appetite for risk, various psychological elements come into play – generally known as tolerance to loss.

For example, do you panic at the first sign of a market downturn, or are you a sheep who follows others?

Your ability to absorb losses without affecting your financial plans is also very important. This is your capacity for loss.

Whatever your disposition, understanding the different types of risks and how much risk you are willing to take is vital before we can recommend suitable options or products to invest in.

WHAT IS DIVERSIFICATION?

When it comes to the weekly shop, putting all your eggs in one basket is a bad idea. It's an even worse idea when it comes to your investments. For example, using all your capital – or even a large chunk of your capital – to buy shares in a single company can be a recipe for disaster.

As we've seen in recent years, even the largest and most stable looking business might run into problems, potentially rendering your investment worthless.

Diversification involves spreading your investments across a number of different asset classes. This can be the first and most important step in spreading, and so reducing, the risk.

By diversifying your investments, the theory is that when one asset fails because of market conditions, others will be on the way up for the same reasons – known as 'non-correlation'.

Many people's investment portfolios feature a diverse mix of commodities, property, futures and other financial derivatives, and in some cases risky cryptocurrencies.

CHOOSING THE RIGHT MIX

To benefit from a diversified portfolio and hopefully outstrip the pace of inflation in 2022, you should invest in assets which behave differently to each other.

The performance of most assets affects the others. It can, for example, be a good time to invest in gold when stock markets are plummeting, as the prices often increase when markets fail.

Not only will choosing the right mix of investments spread the risk, it will reduce the potential for losses.

If you have all your investments in one business, asset, sector or region, you will be exposed if they drop in value.

If you have a conservative attitude to risk, a diverse mix of investments might look something like 50% cash-like instruments, 30% bonds or gilts, 14% domestic stocks, and 6% foreign stocks.

A riskier investor might have a portfolio that has something like 75% in equities, 15% in bonds or gilts and 10% in speculative investments, although that's not for the faint-hearted.

The right selection of assets will vary depending on your individual circumstances, your saving goals, your timescale, and the level of risk you're happy with.

It usually makes sense to reduce your level of risk as you get closer to your goal. For example, if you're a few years away from retirement and have built up enough savings to live on comfortably, you want to make sure that pot is protected from any shocks as it won't have time to recover.

LOOK TO THE LONG-TERM

It's possible to profit from those market fluctuations by investing when a market is in a trough, and selling when it hits a peak.

In practice, however, it's impossible to predict just when those peaks and troughs are coming. Selling assets can result in you 'crystallising' a loss and missing out on any recovery.

Think of investing for a minimum of five years. This can offset any market fluctuations, and let the underlying growth in the value of your investment work for you.

With stock markets, the price of investments will rise and fall. When markets are volatile, the ups and downs can be alarming and those who hold their nerve usually fare best in the long run.

If you're looking to start investing in 2022 to try and outperform inflation, protecting your capital is at the core of what we do.

We can help you understand your attitude to risk and work with you to create a diverse long-term strategy.

Get in touch to develop the investment strategy you need.