Inflation and market volatility

As inflation soars and the stock market drops, here’s a math equation that could help ease concerns.

Let’s take a look at a historical investment calculator*. Back in 2005, you could have started investing just $10 a week in your retirement account, which means you had saved $10 a week for 52 weeks a year…that’s a total of $520. And you could keep doing it annually.

But in 2008, when the Great Recession hit, the federal government bailed out the banks. It caused the S&P 500 to plunge by almost 39%*. For perspective, that’s roughly twice as much as we’ve seen this year.

At that point, you had invested $520 a year for four years. A total of $2,080. With that 39% drop, though, your $2,080 had shrunk to barely $1,500. On paper, you had lost about 25% of your money. But let’s say you kept investing $10 a week. And soon, things started to recover.

One year after the bank bailout—your fifth year of saving $10 a week—you had now set aside a total of $2,600. That year, the S&P 500 jumped by 24%*. That meant your $2,600 was now worth $2,430 on paper.

So you kept investing $10 a week. Sometimes the market went up. Sometimes it went down. But after a decade, the market had increased by a total of 7.7%*. You had invested $5,200 during a 10-year stretch, and on paper, it was now worth almost $8,000*.

It’s important to note that past performance doesn’t guarantee future performance. Investing involves risk, and there’s always a chance you could lose everything you invest**. But what’s happening now is just a snapshot in time. It’s like you’re climbing a mountain and you reach a cliff. You might have to turn around, but you’ll never go all the way back down.

So as today’s economic uncertainty deepens, stick with your plan. And talk to a financial planner who can tailor ways that could help you avoid that cliff.

Inflation risk—How being too safe can be risky

Inflation makes things cost more than they used to. It’s why the average cost of a new car in 1970 was about $3,000 and today, it’s about $36,000. The average price of bread was 25 cents, while today it’s $2.12. If inflation averages 3% a year, in 30 years, groceries that cost $100 today will cost $250. As a smart investor, your goal should be to choose investments that don’t just keep pace with inflation, but have the potential to exceed it.

To understand the real return on your investment, you need to subtract the inflation rate from the investment growth rate. For example, if you get a 5% after-tax return and the inflation rate is 3%, your real return is 2%. Inflation risk isn’t the risk of inflation; it’s the risk that inflation will be higher than you anticipated.

One potential way to reduce your inflation risk is to increase your market risk by adding stocks to your portfolio. Although past performance is not a guarantee of future results, historically, stocks often provide returns higher than the average inflation rate. Having a percentage of your retirement savings in equity-based investments that align with your goals and time horizon could help to increase your purchasing power and offset the effects of inflation.

Playing it too safe by investing only in investments with consistent, low returns, can actually be a very risky strategy due to inflation. Balancing other types of risk with an appropriate asset allocation strategy could help you beat inflation over the long haul.

Read more from TIAA about how you can cope with inflation in your portfolio.

Visit Voya’s Retire Better Blog for other types of money management strategies during inflationary times.

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*Source: https://financial-calculators.com/historical-investment-calculator
**Every reader should take their own personal situation in consideration with talking to their advisor.
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¹ The People History Comparison of Prices Over 90 Years (https://www.thepeoplehistory.com/70yearsofpricechange.html)

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