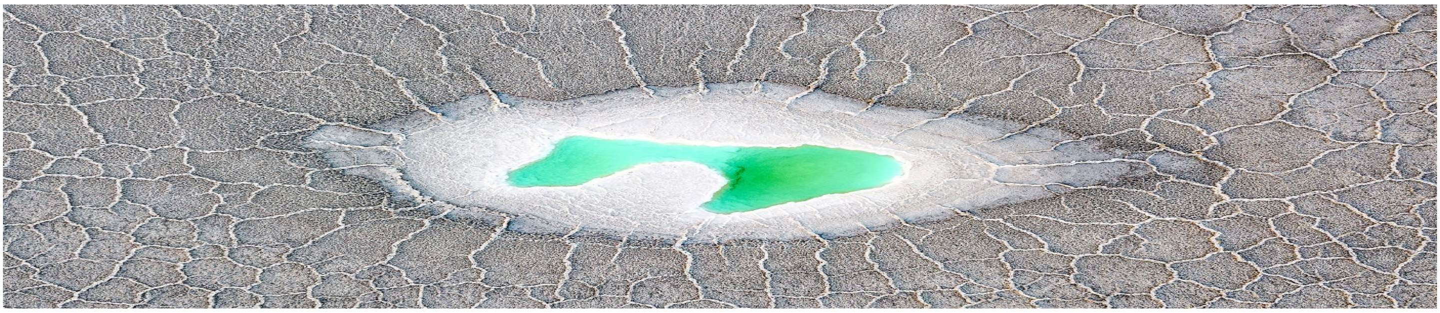

How does inflation affect savings?

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The current price surge has not only been felt in the wallets of private consumers. Together with the interest rate hikes designed to curb it, inflation also affects financial returns and the stock and property markets.

Rising oil prices, a shortage of electronic components and raw materials, and the increased cost of transporting goods are just some of the reasons behind the current price surge, the effects of which are not limited to household purchasing power alone.

The situation is such that it has prompted central banks – whose main task is to maintain price stability – to take action to counter general inflation. Faced with signs of an overheating economy (slowing growth and high levels of inflation), the US Federal Reserve (Fed) and the European Central Bank (ECB) have decided to raise their interest rates in an effort to regulate it.

The purpose of this strategy is to restrict companies' and households' access to credit, and thereby their investment capacity, thus regulating economic activity. This strong and sustained inflation and the resulting rise in interest rates, are not, however, without repercussions for household wealth.

What consequences does inflation have for savers?

The primary impact for savers is a **lower real financial yield.** A distinction should be made between real yields and the posted return on a financial investment. If a passbook savings account pays interest at a rate of 3%, the real yield won't necessarily be 3%. It may even be negative if inflation is above 3%[1] at the same time because, just as they affect your purchasing power, price rises will reduce your "savings power" by decreasing the real return on your investment.

The second negative impact is **a fall on the equity markets,** which are supposed to reflect economic changes affecting businesses over the long term. First of all, inflation can weigh on a company's financial results if its sales prices fail to reflect any price rises it undergoes (commodities, rents, wages, etc.).
In addition, many investors calculate the value of a company by estimating the amount of profit-generating potential taking into consideration its growth, prospects and the economic context. This method is based on the principle that the time value of money[2] changes depending on inflation and interest rates. In this context, rate rises mean a higher cost of time, which will reduce the value of the company as estimated by investors, and therefore of its shares.

Investors looking for a "safer" return may prefer interest-bearing investments made more attractive by the rise in interest rates, such as certain bonds – loans issued by a State or a company to finance their development in exchange for remuneration.

In addition, this increase in rates will cause the **cost of credit to rise:**

- For companies, this will affect their borrowing capacity and therefore their investments and development, which can weaken their stock market value;
- For households, this will weigh not only on their ability to consume but also on their ability to borrow, particularly in terms of housing. This can ultimately result in **a drop in property market prices.**

Another obstacle is **the decline in the value of bonds,** since bond prices fall as interest rates rise.

Understanding why bond prices fall when interest rates rise

Is it possible to use inflation to your advantage and, if so, how?

In an environment of high inflation, preference should be given to investing in the shares of companies capable of benefitting from price rises or which are less sensitive to them. Investing in the luxury sector can, for example, be an attractive option when price is not a deciding factor in purchases for the clients of these companies.

Regarding bonds, commodity price rises can increase the appeal of lending to companies involved in producing or trading those commodities.

It is also possible to select products that protect your investments from various risks, such as inflation. But such instruments (known as “derivatives”) require some expertise.

The current context of price rises is likely to last, especially if it leads to widespread wage increases. Although central banks are working to limit the effects, the situation is not without difficulty for households and their assets.

Faced with such an environment,

active[3] and diversified management of savings has many advantages thanks to its ability to diversify investments and select investment opportunities.

[1]The real yield corresponds to the posted interest rate less inflation.

[2]100 euro does not buy the same quantity of goods today as it did 20 years ago because the prices of these goods have changed in the meantime.

[3]Active management entails selecting the financial assets (equities, bonds, currencies, etc.) that will generate the best performance in relative terms, and buying at the right time. By contrast, passive management involves seeking to replicate a stock market index.

Important legal information