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# Inflation Worries Are in the Air

*What you need to know about the rising cost of living*

By KAREN HUBE

GAS PRICES, as of October, were up 50 percent compared with a year ago. Used cars cost 26 percent more. Hamburger meat ran you 13 percent more than it did the previous fall. Americans are facing some of the steepest price increases in over a decade. Three-quarters of people retirement age say the rise in prices has hurt their finances, according to the financial website Bankrate.

It's unnerving. Inflation, which is the rate of increase in overall prices, poses a major threat to your long-term financial security, eating away at the purchasing power of your dollars.

But don't panic just yet. Instead, learn how to put current trends into perspective and how to limit inflation's impact on your finances.

## 1 The spike will likely settle

The standard measure of inflation in the U.S. is the Bureau of Labor Statistics' Consumer Price Index (CPI), which tracks price changes on a basket of goods and services, including food, housing, energy and health care.

In October, the CPI was up 6.2 percent year over year—far above the average annual rate of 1.75 percent in the 10 years ending in 2020.

Why the jump? Relaxed pandemic restrictions earlier in 2021 unleashed pent-up consumer spending, says Wade Pfau, professor of retirement income at the American College of Financial Services. Rising demand typically causes an uptick in prices; so do shortages of raw materials and transportation bottlenecks, which also emerged during the pandemic.

The general expectation among economists last fall—subject, like all economic forecasts, to revision—was that the inflation rate will drift back down, probably starting in 2022. "We expect that inflation is going to moderate over the medium term to something closer to our target of 2 percent over the next couple of years," says Charles Gascon, senior economist at the Federal Reserve Bank of St. Louis. "While prices may not all come back down, they should generally stabilize." Pricing pressures seemed to be easing this past summer: Month-over-month CPI increases fell from a 0.9 percent rise in June to 0.3 percent in August and then to 0.4 percent in September. But the inflation index then rose 0.9 percent in October, driven by higher prices for energy, shelter, food and motor vehicles.

## 2 This inflation is different

In the late 1970s, as inflation soared—it peaked at over 14 percent in 1980—savers could park their money in relative safety and still keep up with rising prices. In January 1978, for example, when prices were up 6.8 percent over the previous year, you could get a 6.4 percent yield on a money market fund backed by bank certificates of deposit and short-term U.S. government debt. Yields on savings kept up with inflation. That's clearly not happening today, with

savings accounts and six-month CDs paying a fraction of 1 percent. But why? The short answer, Gascon explains, is that the factors driving inflation back then were different from those at work now.

The longer answer: In the 1970s, he says, when a strong economy was driving a broad array of prices upward and inflation expectations were high, the Federal Reserve raised rates so that people had an incentive to save. The hope was that demand growth would slow, prices would stabilize and inflation would subside.

Because prices have been relatively stable over the past few decades, Gascon adds, inflation expectations are lower and the Fed's policymakers are working under the assumption that what's currently driving inflation is pandemic-related and temporary. For now, they see no need to rapidly raise short-term interest rates, which would raise savings account interest rates—but would also risk slowing jobs growth and the overall economy.

## 3 Smart spending can balance your budget

If you're planning a big cash outlay, consider waiting for prices to settle down, says Mark Zandi, chief economist at Moody's Analytics. "Delay spending on items that are experiencing a big spike in price, like a car," he notes. "The same goes for home improvements. Prices for lumber and materials are still above normal, and labor costs are high."

Selectivity at the grocery store is important, too. In October, overall food prices were up 5.3 percent over the prior year, but the per-item inflation rate had big variations. For example, prices soared more than 20 percent for steak and bacon, but just 6.8 percent for whole chickens. "You have to change your day-to-day decisions" to keep your food costs steady, Zandi says.

## 4 Social Security can help

The 2022 cost-of-living adjustment (COLA) for Social Security, effective in January, is 5.9 percent. That adds $92 to the $1,565 monthly payment that the average retired worker would otherwise receive—an increase of about $1,100 per year.

If you're receiving Social Security benefits, it's reasonable to expect that January's increase will help your income catch up to your expenses. The COLA is based on a slightly different measure of inflation that's running higher than the more closely tracked CPI. A separate government measure of inflation aligned to the spending of people 62 and up indicates that costs for older Americans are rising at a slower rate than those other measures. Another good sign: Medicare forecasts that average drug-plan premiums will rise less than 5 percent in 2022.

## 5 You can protect against the long-term impact

If you have retirement savings, the key to keeping up with inflation, according to financial advisers, is to invest a good part of that money in the stock market. Nothing is ever guaranteed, and markets can fall precipitously. But the total return of the S&P 500—an index of most of the largest publicly traded U.S. companies—has averaged more than 10 percent per year since its 1957 launch, far exceeding the 3 percent average inflation rate.

You can also fight inflation with U.S. savings bonds. If you buy a Series I bond before the end of April, you'll get a guaranteed rate of 7.12 percent for the first six months. The rate on your bond, linked to inflation, will reset up or down every six months. Electronic purchases of I bonds are limited to $10,000 per person annually. Another anti-inflation tool, Treasury Inflation-Protected Securities (TIPS), has no such limit but has a lower effective yield. (To learn more or to make a purchase, go to treasurydirect.gov.)

Assuming you have an adequate emergency fund in ready cash, James Regan, an adviser at SharpePoint in Phoenix, suggests a portfolio that's mainly a broadly diversified stock mutual fund plus a fixed-income bond fund with an emphasis on TIPS.

One investment that's less likely to protect you is gold, which is often pitched to nervous investors. "Gold is not an inflation hedge," Regan says. An ounce of gold, worth $1,860 in November, was worth about $2,170, adjusted for inflation, in 2011. "If you bought gold 10 years ago," he says, "you'd be underwater today." *—With reporting by Gabriel Baumgaertner*

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## Up-and-Down Costs

Here's how much prices for some goods have risen—or even fallen—over the past two years