Ros Altmann: It's time to get serious about inflation

By **Ros Altmann** | 29th March 2021 4:55 pm

Despite the double whammy of Covid and Brexit, financial markets have stood up surprisingly well.

Much of the underpinning for asset markets has come from policy, rather than the economy. Thanks to devastated industries such as hospitality, travel and exports, the economy is about 9 per cent smaller than this time last year. However, equities are near their highs.

Ever-expanding quantitative easing programmes have allowed governments to offer previously unthinkable levels of financial support for jobs and companies.

But the scale of money creation and reliance on debt to boost short-term growth leaves many unanswered questions — in particular, around the risks of debt default and inflation. Indeed, there are clear risks of inflation ahead. Thus far, the inflation has been in the asset markets, rather than the goods markets.

Central banks, governments and financial markets seem hooked on QE support. QE was meant to be a temporary policy back in 2008, with the 'temporary' injections being withdrawn once growth stabilised. Yet, despite rising post-2009 growth, record pre-pandemic job levels and negative impacts on savers and pensions, it continued.

The pandemic saw it vastly expanded, with the government's £400bn borrowing neatly offset by Bank of England balance-sheet expansion of similar magnitude.

This supports growth and the government's aims for investment-led recovery, but it has also directly injected money for individuals.

Chancellor Rishi Sunak's recent Budget announced a St Augustinian approach to fixing the fiscal deficit: spend huge sums now while promising tax rises to pay for it later. Like QE, however, this leaves flexibility to adjust the timescale and detail of future fiscal measures or abandon tax rises altogether, thereby possibly compounding future inflationary pressures.

Given the extreme scale of accumulating debt, perhaps a bout of inflation will be an attractive means of avoiding default. With QE money effectively underpinning the direct boost to households and corporate spending, on top of the original indirect stimulus of rising asset prices, the risk to consumer prices is magnified.

How can savers and pensioners protect themselves? Inflation-linked bond yields appear negative and fixed income interest payments (except the most risky) will not match overshooting inflation.

To address such risks may require more investors to embrace diversification into infrastructure, commodities, property and other real assets. Pension assets could help boost green growth and finance new housing, while offering some hedge against rising inflation risks.

Asset bubbles and inflation can take investors by surprise. It is time to heed the warning signs.

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