

Weathering the inflation storm

Is it time to diversify your portfolio?

The mantra ‘Cash is king’ has echoed through the investment world for years. Cash forms the backbone of our society – it pays for our purchases, settles our debts and serves as a liquid asset in tough times.

As long as money spins the globe, many will uphold cash as the reigning monarch. However, this crown has been slipping off lately. This raises a question – is it wise to lock into a rate that incurs losses in real terms merely to avoid the short-term volatility of financial markets?

THE VALUE OF CASH DIMINISHES

The circumstances for each saver are unique. But the argument for holding cash over investments, especially over the longer term, simply because savings rates are on the rise, is flawed. In the face of still high inflation, the value of cash diminishes, while investments can potentially offer higher returns. Therefore, evaluating whether holding on to cash is the best strategy, especially in the long run, is essential.

With inflation showing only muted signs of letting up, the real worth of your wealth held in cash may continue to be chipped away. The dilemma then lies in figuring out what proportion of cash should remain in the bank, exposed to inflation, and what portion should be invested.

INCOME SECURITY AND LIVING COSTS

Deciding on the amount of cash to retain in the bank and the amount to invest with the aim of outpacing inflation is a complex and highly individual decision. What works for one person might be entirely unsuitable for another, hence the importance of receiving professional advice.

If you depend on employment income to cover living expenses, it may be prudent to maintain a larger cash buffer in case of job loss. Conversely, those with a guaranteed income, such as a final salary pension, might benefit from investing more and banking less. Your living costs also play a role. Those

with higher expenses might prefer to have more saved on deposit for emergencies, especially given the rising cost of living.

LIFE STAGE AND SHORT-TERM EXPENDITURE

Your life stage may also influence your decision. For example, individuals with dependents and a mortgage might prefer to have more banked on deposit for unexpected events than those with fewer responsibilities. Any planned capital expenditure in the next three years (like property purchases or gifting adult children) should be reserved in cash.

COMFORT LEVELS WITH RISK

Regardless of wealth level, some people may find comfort in having a sum of cash in the bank. But it’s worth considering whether keeping excess money in the bank, thus subjecting it to inflation, can be a higher-risk strategy than investing in a diversified portfolio. This is because when inflation outstrips interest rates, the value of cash diminishes, while the value of an investment portfolio has the potential to increase over time. ■

READY TO DISCUSS YOUR OPTIONS?

There’s no one-size-fits-all answer to the question of how much money is too much to keep in the bank. The appropriate amount varies greatly depending on numerous factors. To discuss your options or to find out more, please get in touch with us.

THIS ARTICLE DOES NOT CONSTITUTE TAX OR LEGAL ADVICE AND SHOULD NOT BE RELIED UPON AS SUCH. TAX TREATMENT DEPENDS ON THE INDIVIDUAL CIRCUMSTANCES OF EACH CLIENT AND MAY BE SUBJECT TO CHANGE IN THE FUTURE. FOR GUIDANCE, SEEK PROFESSIONAL ADVICE.

THE VALUE OF YOUR INVESTMENTS (AND ANY INCOME FROM THEM) CAN GO DOWN AS WELL AS UP, WHICH WOULD HAVE AN IMPACT ON THE LEVEL OF PENSION BENEFITS AVAILABLE.

