Heartwood
Wealth Management

Is inflation going to be an issue within the next few years?

Presented by: Emmanuel Moll

Americans are getting stronger. Twenty years ago, it took two people to carry ten dollars' worth of groceries. Today, a five-year-old can do it.

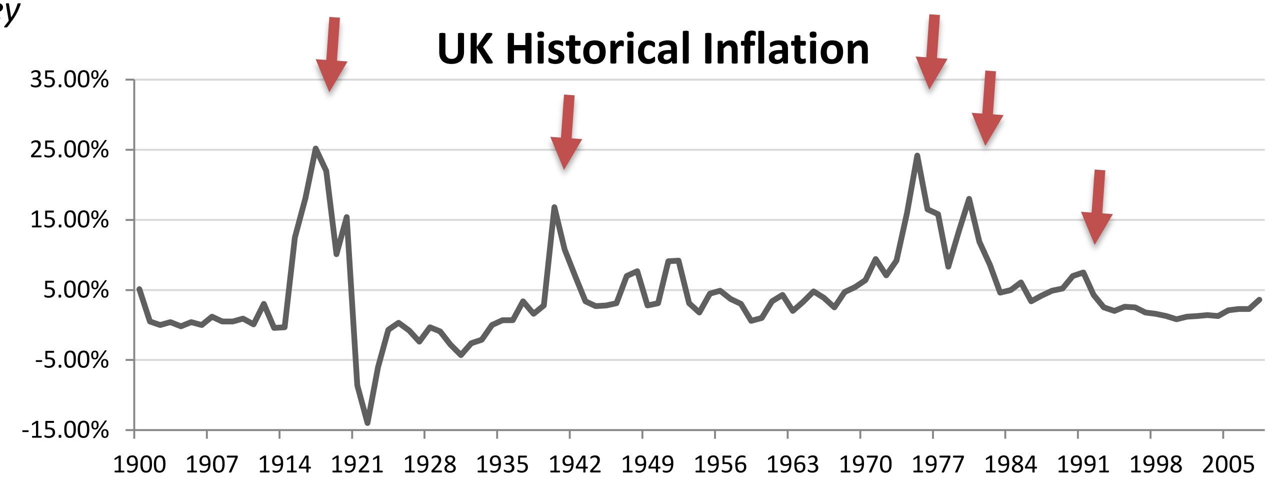
–Henny Youngman

Development

- Background on inflation
- Today's situation
- What the future entails
- What can be done

What are we expecting over for the next years?

Inflation: *a rise in the general price level that results in a decline in the purchasing power of money*

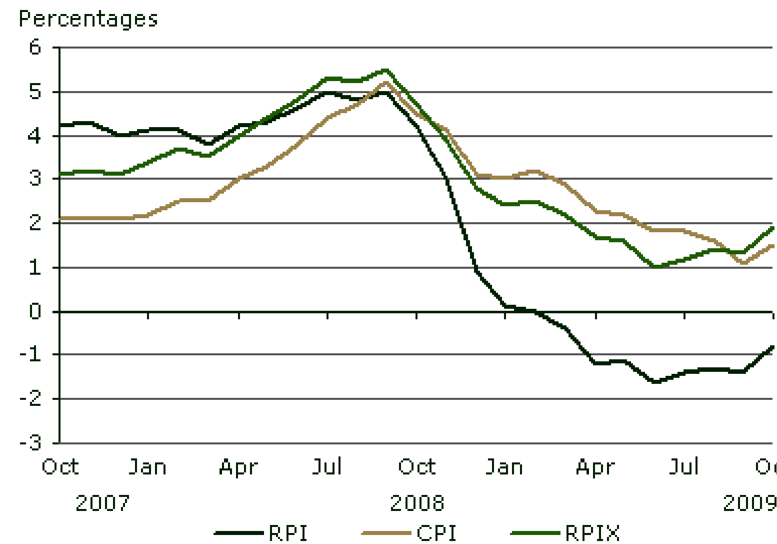


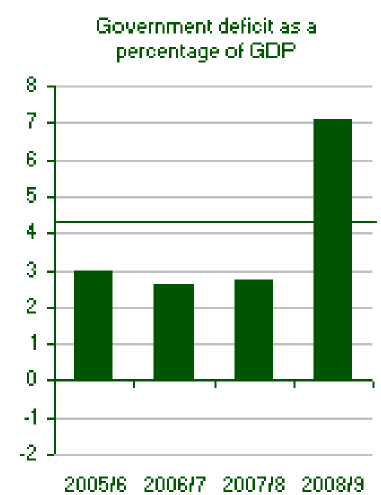
Source: Office for National Statistics

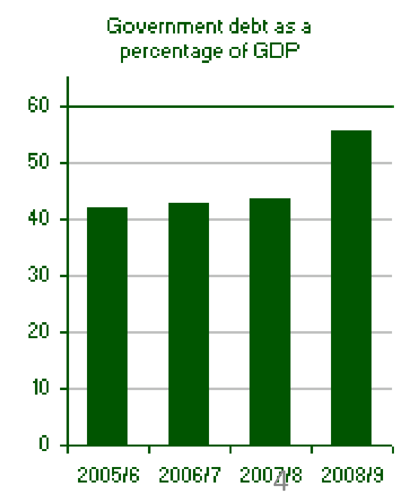
- Inflation is caused by different factors:
  - 1914s: first world war and increase in demand
  - 1940s: inflation driven by demand for reconstruction and new issue of notes
  - 1970s: inflation driven by oil prices affecting the CPI
  - 1980s: cost-push inflation (oil and wage)
  - 1990s: UK (briefly) joins the EU Exchange Rate Mechanism
- Historical events do not lead to inflation on their own, economies policies are an explanation
- Clearly, Government and Central Banks have tools to control inflation, but only a short history of using them the right way (1990s, 2000s).

What is happening today that impacts inflation?

- Worldwide:
  - Oil price increase
  - Rise in food prices
  - Dubai is defaulting on payments
- UK:
  - Quantitative easing
  - Value of the Pound slashed
  - Positive CPI
  - Mortgage drought + spare cash
  - Low Central Bank rates
- Financial markets:
  - Long-term bond yield curve has risen (Source: Brown Advisory)
  - Increased interest in venture capital in fast growth sectors like telecommunications, green technology and clean-technology (Source: PwC)
  - Rise in Gold Price







Source: Office for National Statistics

What the future entails…

- Inflation will take place
- Unknown: rate of inflation
    - Central Bank will try and keep it low (2%)
    - Try to avoid liquidity trap

	HIGH INFLATION	**‘REGULAR’ INFLATION**
SIGNS	- Increase in monetary base - Rise in commodity prices	- CPI inflation is low (1.5%) - RPI is negative - Economy not benefitting quant easing
IMPACT	- Variable rate borrowers - Fixed income - UK, US, EU currency holders - Lenders on fixed rate	- Investors in commodities - Fixed rate borrowers - UK government’s high debt - Lenders on variable rate
WHEN	- When the banks’ extra liquidity flows through the system i.e. when lending resumes (= higher velocity of money)	- Now

What does it mean for the global economy and Heartwood?

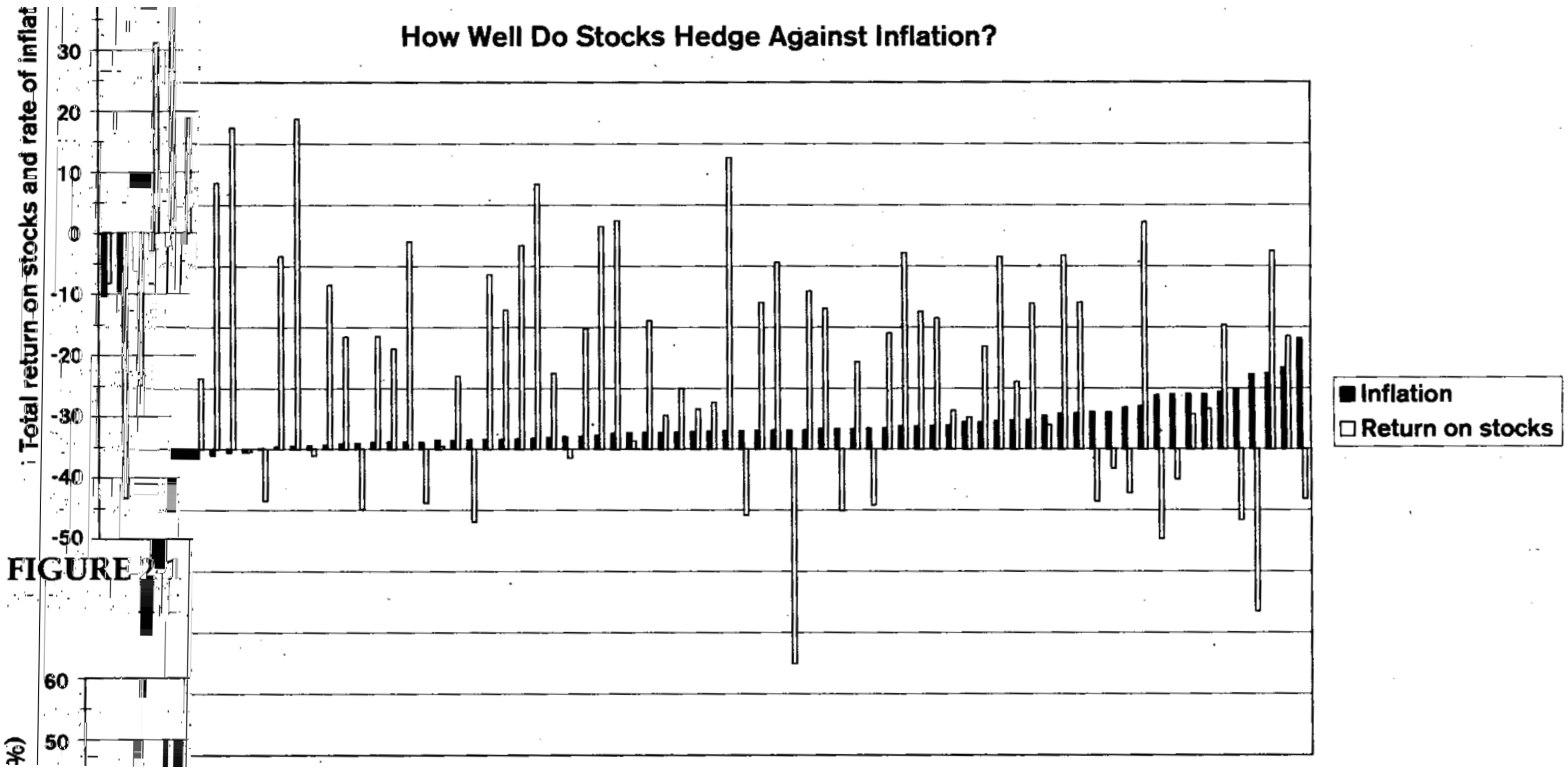
- Global economy:
  - High volatility as the outlook for inflation increases and decreases
  - Decrease in industrial output as planning becomes precarious
  - Increase in unemployment
  - Devaluation risk for leading currencies ($,£,€)
  - Wealth transfer to growth economies
- Heartwood:
  - Erosion of capital for fixed income clients
  - Change in Asset allocation
  - Investments in asset classes that can profit from inflation
    - Divest from £ and $ into other currencies (especially resources-rich countries)
    - REIT
    - Alternative assets: wine, coins & commodities
    - UK equivalent of US TIPS (Treasury Inflation-Protected Securities)
    - Gold

Conclusion

- Inflation is driven by economic actions resulting (or not) from exceptional events
- Major factors driving inflations are:
  - Rise in commodity prices (cost-push)
  - Increase in monetary base (demand-pull)
- These factors exist today and inflation will thus occur though its rate is unknown
- Consequences of inflation include a loss of monetary value
- For low inflation, a shift in asset classes will hedge inflation
- But will the government do anything about it….

"By a continuing process of inflation, government can confiscate, secretly and unobserved, an important part of the wealth of their citizens." -- John Maynard Keyens

Are stocks good enough alone?



Source: *The Intelligent Investor*