

PLANNING

Understanding the inflation factor

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September's 3.8% inflation rate was probably the peak. How does it affect your planning?

The rate of inflation is one economic number that is familiar to most people. Every month, usually on a middle Wednesday, the Office for National Statistics (ONS) releases the latest Consumer Prices Index (CPI) along with a raft of other inflation statistics. The focus is always on one piece of the ONS data dump, the yearly CPI inflation rate. Since the start of the decade it has ranged between 0.2% and 11.1%, while the current consensus is that after peaking in September 2025, inflation will fall in 2026.

For all the attention that it receives, yearly CPI inflation is poorly understood. For example:

- It is a gauge of the 12-month difference in the overall price of a basket of 752 goods and services. So, the October 2025 inflation rate shows how much higher prices are than in October 2024.

- While food price inflation grabs the headlines, 'Food (and non-alcoholic drinks)' is only the fifth largest of the CPI's twelve price sectors. The largest, at nearly 15% of the index, is 'Recreation and culture'.

- The CPI takes no account of mortgage interest or other costs associated with home ownership. There is an inflation index which covers owner occupied housing costs, CPIH, but it is not widely used. In October 2025, yearly CPIH inflation was 3.8%, 0.2% higher than annual CPI inflation.

- A falling rate of inflation means that price growth is slowing – it does not mean that prices are falling.

LONG-TERM IMPACT

That final point is key to understanding the long-term impact of inflation. While the price of individual items in the CPI can go up and down, it is extremely rare for the overall CPI to drop over the year. You can see this in the graph below, where the purple line is yearly CPI inflation and the grey area is the cumulative

rise in prices since January 2020. The 2022 surge in inflation pushed up the cumulative increase, but as annual inflation declined, the cumulative figure kept on heading upwards, albeit not so steeply.

CUMULATIVE RISE OF 30%

The result is that as the end of 2025 approaches, overall prices (based on October's CPI) are almost 30% higher than in January 2020 – an effective average yearly inflation rate of 5.5%. Those numbers have important consequences for your financial planning:

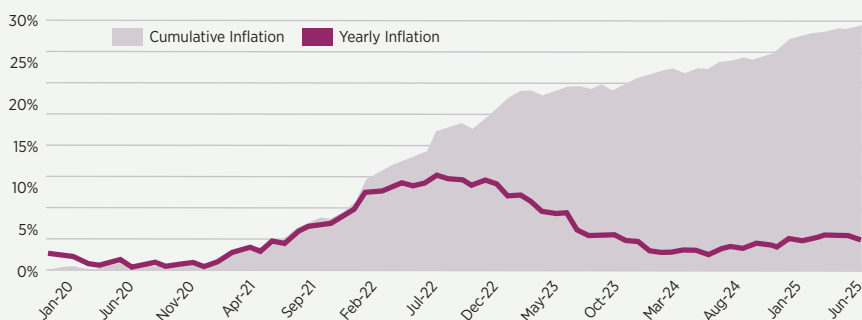
- All other things being equal, any life cover or income protection that you have in place should be at a level 30% higher than it was at the start of 2020. If all other things are not equal – changed family circumstances, for instance – the increase may need to be greater.
- Your retirement planning and other future savings goals probably need to be reviewed and contributions increased. When they were set up, it is unlikely an allowance was made for the inflation of the past half decade.

Even though inflation outlook has improved, do not think that because it now appears to be on the way down you can ignore inflation's past effects.

❖ *The value of your investment and the income from it can go down as well as up and you may not get back the full amount you invested.*

Past performance is not a reliable indicator of future performance.

CPI INFLATION FROM JANUARY 2020



Source: ONS