

***LIFEFLATION* - THE OUTSIZED INFLATION YOU (N)EVER KNEW EXISTED**

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April 19, 2024

Part 1: *Lifeflation*—The Inflation of Modernized Life

Inflation has defined our current decade, with CPI rising by 20.8% cumulatively or 4.6% annually over the last 4 1/3 years—double the 2.1% rate in the previous two decades.



Painful enough?

Actually, it's worse! CPI is just the visible tip of the inflation iceberg.

What's the real inflation rate?

Consider these vignettes from our client experiences. Each might seem anecdotal, but collectively, they reveal a larger truth.

Four years ago, my family's favorite meal at an SF restaurant cost \$202, including \$163 food charges plus a 15% tip and 8.63% tax. Recently, the same meal amounted to \$273, with \$200 allocated to food (a 4.9% annualized increase, roughly in line with the 5.4% annualized increase of the CPI Food & Beverage Index¹ since 2020). Additionally, there were new charges: a \$9.90 "SF health mandate (5%)" and a newly "recommended" 22.5% tip of \$46.80. The total bill grew at an annualized pace of 7.2%, outpacing the CPI's¹ 4.6%

and the Food& Beverage's 5.4% annualized increases.

Redfin² reports that home affordability income requirements have risen 11% annually since 2020, and clients looking to buy into multi-level retirement homes have seen costs climb 8-10% annually over the last five years. In parallel, we have observed the college attendance cost ballooning at over 6% annually for nearly a decade.

Finally, outside of traditional expenditures, there are also the 'catch-ups' of modern life: While the cost of smartphones has seen a relentless sub-5% annualized inflation over the past two decades, the fact that today's teenagers consider smartphones a necessity has introduced an entirely new category of expenses to family budgets that did not exist at the beginning of this century.

The emerging refrain is clear: *Lifeflation*—defined as the inflation rate for not only sustaining but modernizing consumers' standard of living—pushes total inflation into the upper single digits—truly concerning. We doubt this is about to change, and perhaps it has never been different for the same mission. Yet, as we will outline in Part 2, we believe there is an answer to the perennial lifeflation challenge.

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Part 2: Outinvesting Lifflation

Inuit use numerous words to actionably differentiate ice. Similarly, investors must recognize that 'inflation' encompasses drastically different conditions, such as the '70s/'80s demandflation and the post-CoViD supplyflation.

Moreover, there is inflation tracking the cost of maintaining a static standard of living (captured well by the Consumer Price Index/CPI or the Fed's favored Personal Consumption Expenditures/PCE) vis-à-vis 'lifflation' that tracks the cost of adjusting to life's modernization pressures.

While CPI/PCE capture the static components of transportation inflation (fuel, vehicle, insurance, fares, maintenance), lifflation encompasses additional costs like congestion-priced road tolls and the need for pricier alternative-energy cars to cope with worsening traffic.

The pattern is clear: Modernizing life comes with added charges because innovation carries a higher price tag due to its extra development costs, appeal, and rarity.

This realization allows us to pinpoint the main source of lifflation and indirectly estimate its cost:

On the flip side of lifflation's modernization pressure is the economic success of the companies that proliferate innovation, best reflected in their market premium. In this light, the market premium of the innovators simultaneously represents the root cause and the solution to combatting lifflation.

We use the annualized 20-yr. growth-minus-value equity return to estimate the rate of lifflation, which is currently around 4%³.

This pragmatic view of lifflation can help investors neutralize it—by outearning it! However, it's not easy.

With inflation averaging 3% and lifflation 4%, the combined 7% hurdle dwarfs the 10-yr. annualized return of the S&P Target Risk Conservative (+1.07%), Moderate (+1.86%), and Growth (+3.49%) indices and even surpasses the return of the [Aggressive Index](#) (+4.91%). The S&P 500, a narrower growth-tilted US Large Cap Index, has a higher 10-yr. return (+11.61%), but finished the first decade of this century in the red, has a 13% shortfall rate since 1900 (well outside the desired 10% or ideal 5% range), and is prone to bear market collapses.

So, is investors' standard of living destined to erode?



This is clearly [the risk](#) of portfolios positioned conservatively or inflexibly tied to any singular index. Yet innovation drives market advances, which we believe can be harnessed to combat lifflation via a market-adaptive and risk-controlled portfolio that dynamically navigates market regime shifts. This investment approach has guided us for nearly a quarter-century.

¹ Source: YCharts

² Redfin. (2024, March 26). Housing affordability remains near historic lows. Retrieved from <https://www.redfin.com/news/income-needed-to-afford-home-february-2024/#:~:text=Housing%20Affordability%20Remains%20Near%20Historic,below%20October's%20all%2Dtime%20high>

³ Computed as the difference between the 20-yr. annualized return rates of the S&P 500 Growth Index and the S&P 500 Value Index. Data sourced from TC2000/Worden Brothers.

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PM-04222027-6571635.2.1