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# The Long-Goodbye: Diversified Portfolios Designed to Weather Higher for Longer Inflation

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**Since inflation peaked in 2022 in developed nations, central banks have largely succeeded in bringing inflation close to their long-term targets. But progress to 2% has been frustratingly slow. In January, US headline inflation rose slightly to 3% and core inflation that excludes food and energy rose to 3.3%.[1] In Europe, inflation surprised to the upside in January at 2.5%.[2] With the inauguration of the Trump administration in January 2025, the threat of global trade wars and currency volatility could delay rate cuts in the US and Europe.[3] Historically, trade wars have been associated with price inflation, and while much is still uncertain, markets have generally lowered their expectations for rate cuts for the calendar year. In 2025, institutional investment portfolios may experience the challenges of higher interest rates and inflationary pressures.[4]**

During his testimony on February 12th, Chair Powell reminded Congress that the Federal Reserve does not get excited about one or two bad inflation prints and that "We (the Fed) target PCE inflation because we think it is a better measure of inflation."[5] But progress on the inflation fight has been slow in the Fed's preferred measure of inflation as well with the Median PCE (Personal Consumption Expenditure). PCE was 3.2% in December 2024 and core PCE excluding food and energy was 2.8%.[6] In Europe, consumer are not convinced that the European Central Bank will be able to tame price pressures this year.[7] In both the US and Europe, the price of goods has been falling but not enough to offset price pressures from services.[8]

[1] Source: Bureau of Labor Statistics as of February 12. 2025.

[2] Source: European Commission as of February 3, 2025.

[3] Source: Bloomberg, J. Randow et al., "World Inflation at Risk of Rekindling With Trump's Trade War," February 5, 2025.

[4] Ibid.

[5] Source: Financial Times, J. Politi et al., "US Inflation Unexpectedly Increases to 3% in January," February 12, 2025.

[6] Source: Cleavland Federal Reserve "Median PCE inflation" as of February 12, 2025. PCE is a lagging indicator.

[7] Source: Financial Times, O. Storbeck, "ECB Will Not Fully Tame Inflation This Year, Fear European Consumers," January 31, 2025.

[8] Source: Financial Times, J. Politi et al., "US Inflation Unexpectedly Increases to 3% in January," February 12, 2025.

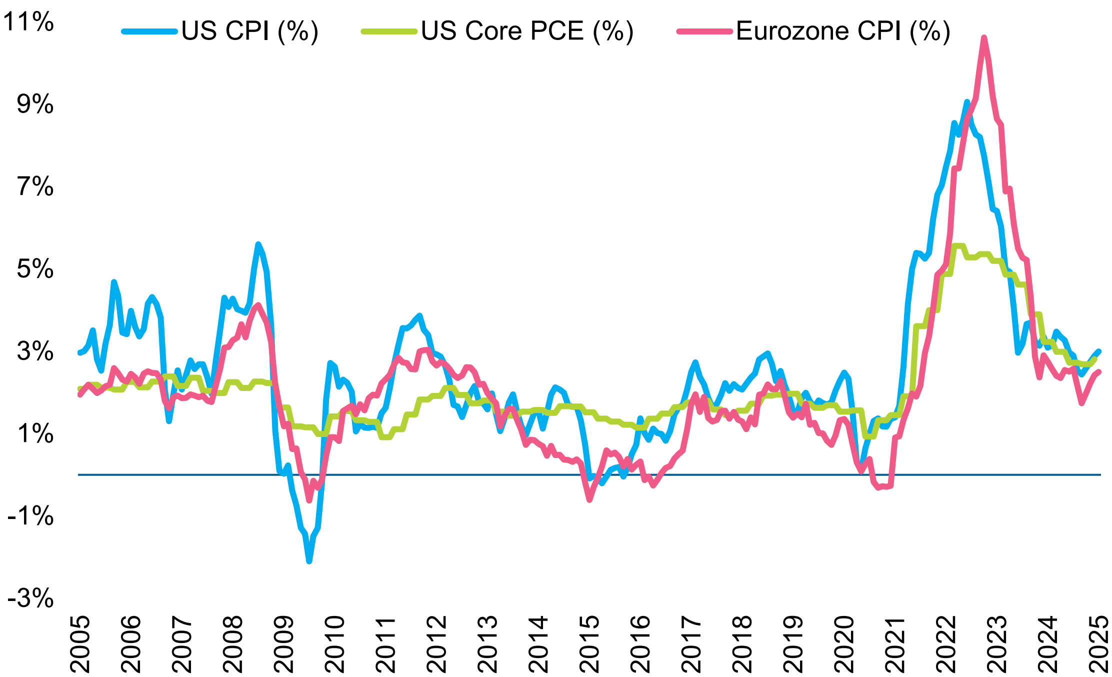


**FIGURE 1**
**Inflation in US & Europe (%)**
Source: Bloomberg as of February 13, 2025.

Inflation can erode real returns for institutional investors, as stakeholders could see purchasing power decline. Inflation can also squeeze profit margins when input costs and wages costs rise, especially when pricing power is weak as consumers seek bargains and delay purchases. Institutional investors with well diversified portfolios that include public and private assets can often offset the negative effects of higher inflation and interest rates. Private credit – especially collateralized credit – may capture rising prices and high or even rising borrowing costs. Private infrastructure – with its long-lead times – and access to rising prices of natural resources – can also potentially help offset higher policy rates and borrowing costs.[9]

[9] Source: Pensions & Investments, V. Gerritsen, "Commentary: Infrastructure as an Inflation Hedge," April 4, 2023.

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