Deutsche Bank
Research

Investing during Stagflation: What happened in the 1970s

#PositiveImpact

Jim Reid
Head of Credit Strategy and Thematic Research

Henry Allen
Research Analyst

With growing fears that we're heading for stagflation, investors are increasingly asking how they should be positioning for such an environment. Unfortunately, the headline takeaways from the 1970s are pretty bad – in real terms it was a terrible decade for equities and bonds across multiple countries. Whilst this decade is young, and the high inflation has only been around for just over a year so far, we can already see similar patterns between how different assets performed in the 1970s and how they've been doing today.

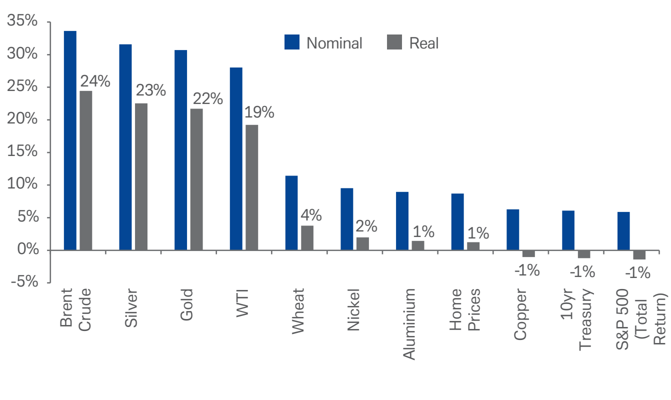
Equities generally saw losses in real terms in the 1970s, but energy was the best place to be on a sectoral basis, echoing 2022's performance. Treasuries declined in real return terms too, although those with shorter-dated yields fared relatively better than their longer-dated counterparts, once again mirroring the 2022 performance. On an international basis there wasn't much respite either. However, the countries who managed to see a positive real performance for equities or bonds over the decade tended to be those who were more successful at keeping inflation out of double digits. For bonds, this correlation between positive real returns and their ability to keep inflation down was very strong.

Another good place to be in the 1970s were precious metals, with gold and silver seeing strong real returns as they lived up to their reputation as an effective inflation hedge. Both have range traded over the last couple of years however. Other commodities did very well in the 1970s, including oil and agricultural goods. That echoes what we've seen in 2022, where commodities are the only asset class to have seen relatively consistent gains this year.

Overall, the main takeaway should be that if inflation stays high for many years, both history and today's high starting valuations suggest it will be very difficult to generate positive real returns in most traditional financial asset classes. Nominal returns will also likely notably underperform their long-term trend. Commodities could be the exception.

Of course, this decade's similarities to the 1970s may fade once tighter policy and a recession push inflation down, and we may return to the lower inflation world that was such a boon for financial assets in recent decades. However, the longer inflation gets entrenched in the system, the more likely inflation stays higher for longer, especially with many of the structural disinflationary forces reversing. As such, it is prudent to look at what happened in this important decade.

Annualised Returns for Selected Financial Market and Commodity Assets During the 1970s



Source: GFD, Haver Analytics, Deutsche Bank

Clients of Deutsche Bank Research can access the full report here.

For important disclosure information please see: https://research.db.com/Research/Disclosures/Disclaimer