M&G wealth

The dash to cash: Why it pays to think longer-term with your client's money

Interest rates have recently been at a 15-year high. That can make it tempting to move a lot of your clients money out of investments and into interest-earning cash savings – such as deposit accounts and cash ISAs.

But a dash to cash may not be the smartest move for your clients money. Long term, keeping money invested in stock market-based investments, could deliver stronger returns. Here are five reasons to consider with your clients.

1. Cash can't keep pace with inflation

Inflation has been a big worry for all of us in recent years. In late 2022, prices were rising at an annual rate of more than 11%, due to factors such as the Ukraine war hitting energy prices and lingering disruption from the COVID-19 lockdown.

Inflation of 11% meant that a weekly supermarket shop costing £100 a year before was now costing around £111.

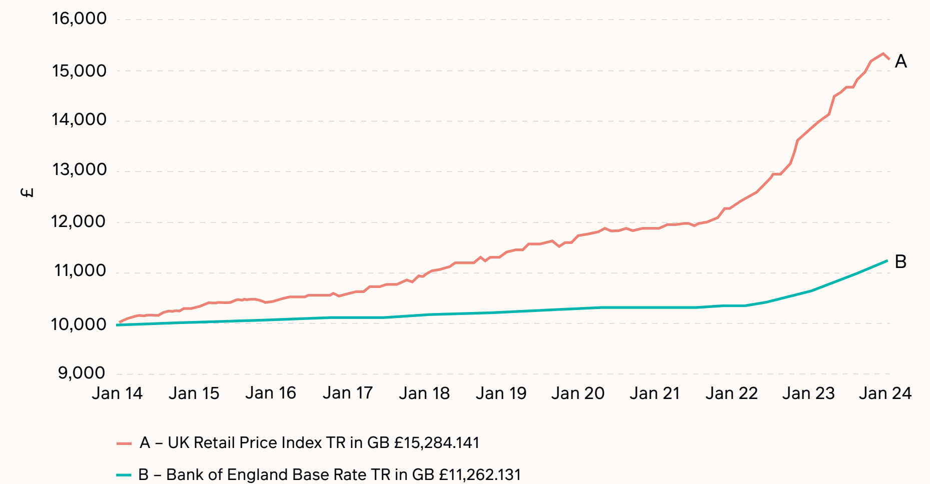
Inflation has fallen sharply since then. But inflation is almost always with us – and effectively means the £1 in our pocket is constantly losing value. Even at the government's target inflation rate of 2%, £1,000 would only be able to buy £906-worth of goods after five years and £820-worth after 10 years.

Rate of annual inflation	Purchasing power of £1,000	
	After 5 years	After 10 years
2%	£906	£820
5%	£784	£614
10%	£621	£386

Source: FE Analytics July 2024

One of the few ways to combat this loss in 'purchasing power' is to hold investments that can potentially grow in value at a faster rate than inflation. Time and time again, assets like shares have been shown to deliver above-inflation growth (partly because they're investing in the companies whose goods and services are rising in price).

By contrast, interest-earning deposits tend to track below the rate of inflation. So although savings deposits can deliver attractive rates in the short term, it's essential to consider what your clients return will be once inflation is taken into account. For example, a £10,000 investment earning 5.25% interest would effectively only be worth £9,875 after a year if inflation is 6.5%



Source: FE Analytics, August 2024

2. Holding a range of asset classes can help optimise and smooth out returns

Another reason for looking beyond cash for your clients, is that different asset classes tend to perform well at different times.

The table below shows the 12-month performance of key asset classes over a 10-year period. We can see that shares were the best performer in three of the 10 periods – and commercial property was the best performer in four periods. Conversely, lower-risk bonds saw good performance in years when those other two asset classes were struggling. Showing you aren't always able to pick the best asset class. However, cash has delivered the worst performance overall as demonstrated in the performance chart below.

Different asset classes and their 12-month performance

Asset Classes	31.07.14 to 31.07.15	31.07.15 to 31.07.16	31.07.16 to 31.07.17	31.07.17 to 31.07.18	31.07.18 to 31.07.19	31.07.19 to 31.07.20	31.07.20 to 31.07.21	31.07.21 to 31.07.22	31.07.22 to 31.07.23	31.07.23 to 31.07.24
Shares – UK All Companies	7.65%	0.92%	14.69%	7.34%	-1.44%	-16.20%	28.98%	-4.12%	3.99%	12.18
Commercial Property – UK Direct Property	11.77%	-1.37%	8.52%	8.08%	1.68%	-5.78%	4.88%	14.22%	-14.39%	-0.63
Corporate Bonds – Sterling Corporate Bond	4.75%	9.58%	2.63%	-0.34%	6.53%	5.48%	2.27%	-12.04%	-6.82%	9.83
Government Bonds – UK Gilt	7.04%	12.67%	-2.68%	0.05%	6.17%	9.05%	-4.98%	-15.30%	-16.73%	4.81
Cash – Deposit & Treasury	0.11%	0.10%	0.27%	0.18%	0.12%	0.01%	0.47%	0.22%	2.62%	4.73

1st (top) 2nd 3rd 4th 5th (lowest)

This key shows the rank of the asset class performance (1st being the top performance and 5th being the lowest) and the actual return is shown within each box.

Source: ABI Pensions Sectors July 2024

Please remember the value of your investment could go down as well as up and you might not get back what you invested and that past performance should not be considered a reliable indicator of future performance.

Multi-asset investing can be an effective way to capture strong performance wherever it arises.

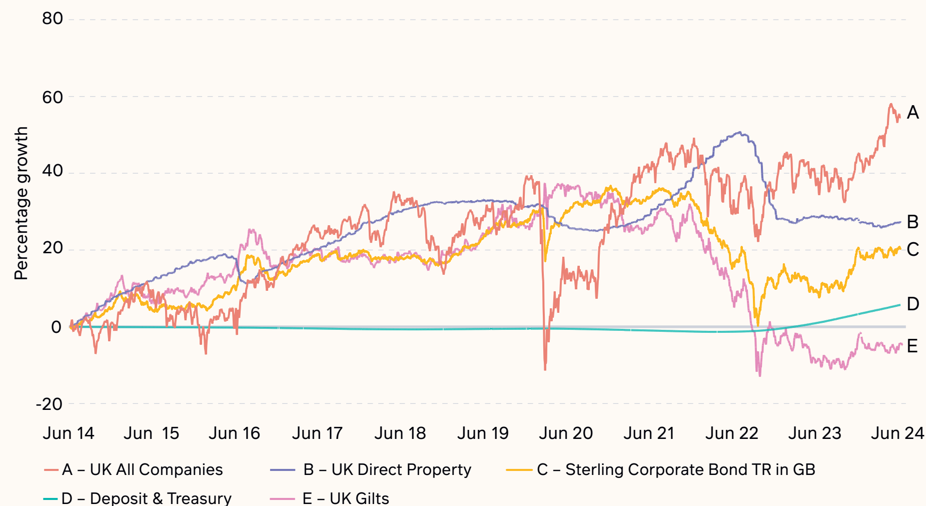
Plus, if your clients are clients are worried about investment volatility, a diversified approach means that any losses in one asset class can potentially be offset by gains in another. This can help the overall performance of their portfolio to enjoy a smoother ride.

3. Being patient can reap rewards

Of course, the ups and downs of the stock market can be a real concern for your clients – and a reason why holding cash can feel very reassuring.

However, if your clients have time to stay invested and are willing to accept the risks, investments like shares and property have been shown to rise most in value over the long term – see graph. Past performance should not be considered a reliable indicator of future performance.

That's why it's important to ask your clients how long they can keep their money invested. As a broad rule of thumb, shares can require five to seven years to ride out short-term market falls. If you think your client might need might need to withdraw money sooner – it may be prudent to hold it in lower-risk bonds or, indeed, cash.



Source: FE FundInfo

This graph shows gross returns for the sector averages from June 2014 to June 2024 from the Association of British Insurers (ABI) Pension universe.

How different asset classes have grown 2014-2024

Many investors take a 'bucket' approach to their savings and investments. Dividing their money into short term (eg, up to three years), medium term (eg, 3-5 years) and long-term (eg, 5-10 years+) tranches and investing each in appropriate assets. Money can be moved between buckets, depending on when you think it might be needed.

In this way, you can ensure you have an all-important rainy-day fund (see panel) – and you're still optimising your clients to potentially beat inflation and capture investment returns over the longer term.

Cash for a rainy day

Holding all your clients spare money in cash may not be a sensible long-term move. But having some easily accessible cash to meet short-term needs is essential – especially emergencies like house and car repairs or periods of unemployment.

As you know advisers often recommend having at least three months' (and ideally up to six months') worth of living expenses as a rainy-day fund.

This can give your clients a reassuring safety cushion. It also makes it less likely that they'll need to pull money out of other investments unexpectedly – for example, just when markets have seen a downturn and investment values have fallen.

4. Savings rates will fall at some point

Just as a crystal ball can't tell us how different investments are likely to perform, no-one can predict exactly what will happen to the interest rates your clients will earn on their savings. Although your clients may be earning a very attractive rate now, you need to consider what rates might be on offer when they come to an end.

We've created this chart to show the Bank of England base rate since the start of the 2000s and how often – and sometimes how quickly – it changes. If the Bank of England decides the threat of inflation has now subsided, it could drop interest rates very sharply.

Again, a properly diversified investment portfolio can help to provide a buffer against that (and, indeed, many investments such as company shares may perform more strongly as lower interest rates benefit their business).

Bank of England base rate since January 2000

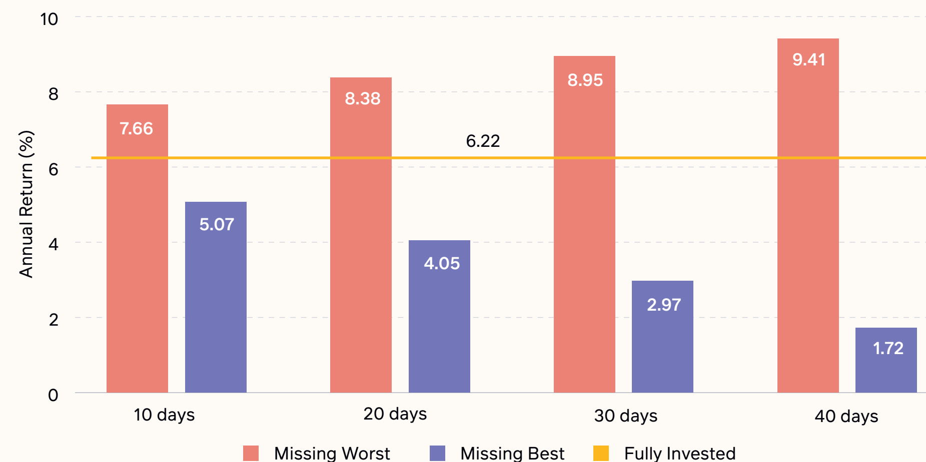
5. Being out of the market can mean missing out

You may be planning to keep most of your clients' capital on deposit – then move back into investments as soon as interest rates start to fall. But trying to time a re-entry into investment markets can be costly.

Lots of analysis has shown that just by missing out on the 10 best individual days in markets, investors can lose most of their return. It can be smarter, then, to keep some capital continually invested to avoid missing out on periods of very strong performance.

The challenge of timing the market

Over the period 30.06.04 to 30.06.24 the annual return for being fully invested is 6.22%, missing the best 10 days reduces it to 5.07%, 20 days is 4.05%, 30 days is 2.97% and 40 days is 1.72%.



Source: FE Analytics. Figures are for ABI Pension UK All Companies sector from 30 June 2004 to 30 June 2024. Figures show gross annualised return and the impact of missing the best and worst days (measured by daily movements in pricing for sector).

In short

Cash deposits certainly have a role to play in investment portfolios and financial planning generally. But there are plenty of risks to allocating too much capital to cash.

By having a well-balanced multi-asset approach – your clients could be well positioned to capture return potential wherever it arises.

Taking a long-term, diversified approach helps to smooth out market ups and downs too.

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