

ABOVE THE FRAY

Outpacing Inflation with Stocks

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US inflation is back in the news of late, as the year-over-year change in the consumer price index is at the highest level since 2023. This may stoke fears of further inflation for many investors.

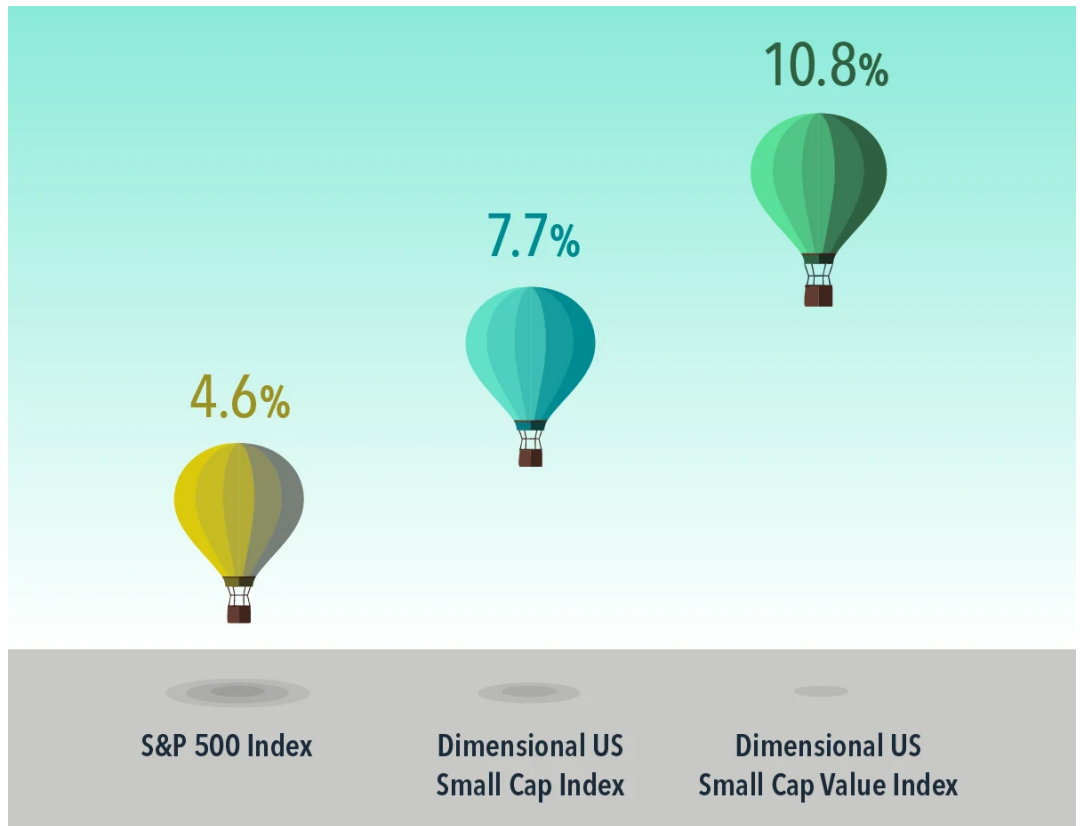
It's important to note that expected inflation is incorporated into the expected returns demanded by market participants. To the extent inflation is expected to impact either future cash flows from an investment, or the discount rate applied to these cash flows, market prices adjust to compensate, resulting in positive expected real returns.¹

This is borne out in historical data. Average real returns for the broad US stock market, based on the S&P 500 Index, have been positive even in years when inflation was above the historical median. Average real returns for small cap and small cap value stocks have been even higher, implying investors should not shy away from tilting toward higher expected return stocks even if inflation expectations are elevated.

We often say one way for investors to deal with inflation is to outpace it. Stocks have been a good way to do this historically.

Exhibit 1**Average Annual Real Returns in Years with Inflation Above the Historical Median**

1928–2025



Past performance is not a guarantee of future results. Actual investment returns may be lower.

In USD. US inflation is the annual rate of change in the consumer price index for all urban consumers (CPI-U, not seasonally adjusted) from the US Bureau of Labor Statistics. Nominal return is the rate of return on an investment without adjusting for inflation. Real return is the rate of return on an investment after adjusting for inflation. Real returns are calculated using the following method: $[(1 + \text{nominal return}) / (1 + \text{inflation rate})] - 1$. The Dimensional indices represent academic concepts that may be used in portfolio construction and are not available for direct investment or for use as a benchmark. Index returns are not representative of actual portfolios and do not reflect costs and fees associated with an actual investment. See "Index Descriptions" in the appendix for descriptions of the Dimensional index data. S&P data © 2026 S&P Dow Jones Indices LLC, a division of S&P Global. Indices are not available for direct investment.

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1. "Real" meaning in excess of inflation.

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