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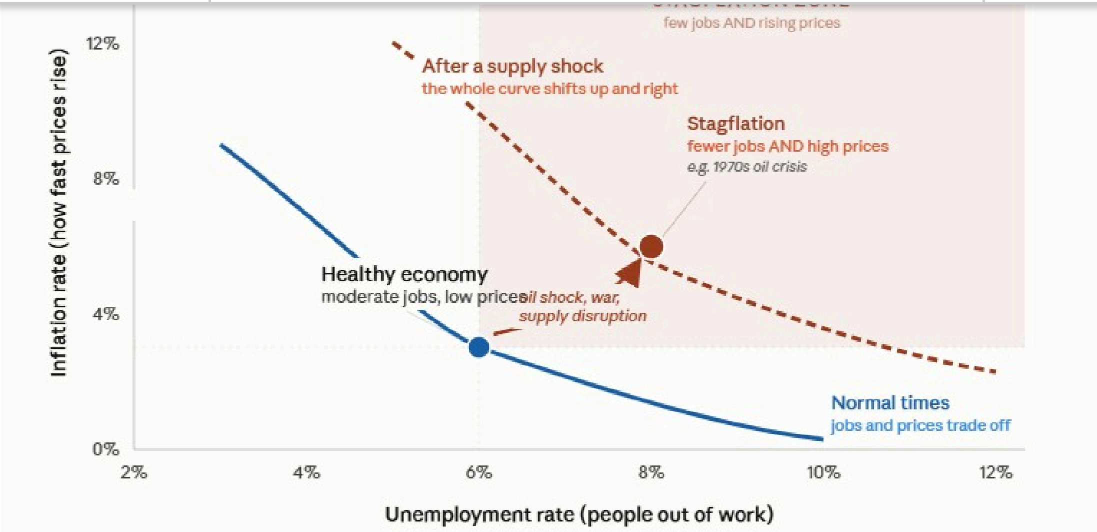
Stagflation: The Economic Storm That Defies the Rulebook

Richard Harris | April 2026

In economics, most problems have a fairly straightforward playbook. If inflation is too high, central banks raise interest rates. If the economy is slowing, they cut rates to stimulate growth. However, occasionally an environment arises that renders these conventional tools ineffective – one where inflation is high, growth stalls, and unemployment rises simultaneously. This is stagflation, arguably the most challenging economic condition any government or central bank can face. With global trade tensions, persistent inflationary pressures, and slowing growth dominating headlines in 2026, we believe that it is a topic worth exploring in this month's newsletter to try and better understand the causes and effects.

The Worst of Both Worlds: Understanding Stagflation

The term "stagflation" combines two words: stagnation and inflation. It describes an economy experiencing sluggish growth, high unemployment, and rising prices at the same time. Normally, inflation and unemployment move in opposite directions – a relationship illustrated by the Phillips Curve, a cornerstone of macroeconomic theory. Stagflation breaks this relationship entirely, leaving policymakers in a bind: raising rates to fight inflation risks deepening the slowdown, while cutting rates to support growth risks fuelling prices further.



Blue curve: when one goes up, the other goes down. Coral curve: both go up together.

Stagflation is typically triggered by supply-side shocks, sudden disruptions that reduce the economy’s ability to produce goods while increasing costs. Common causes include sharp rises in energy prices (such as oil embargoes), excessively expansive monetary or fiscal policy that injects money into the economy without a corresponding increase in output, and misguided trade policies that restrict supply chains and productivity. These factors can create a self-reinforcing cycle in which rising costs lead to reduced output and job losses, even as prices continue to rise. Importantly, stagflation rarely appears suddenly – it usually develops gradually as imbalances accumulate after prolonged periods of easy monetary policy or external shocks.

How Stagflation Hits Economies and Markets

Stagflation affects everyone. Consumers see prices rise while their wages remain flat, so they spend less – and that spending is what keeps economies moving. Businesses are squeezed too: their costs increase, but customers are unwilling to pay more, so profits shrink and job cuts follow. Governments collect less tax, spend more on social support, and face higher borrowing costs if interest rates rise.

Stock markets tend to perform poorly during stagflation. Companies earn less because costs are rising and sales are slowing simultaneously. Higher interest rates make future profits worth less today, dragging share prices down. In the 1970s – the last major stagflation episode – US stocks lost value in real terms for years. Fast-growing companies are usually hit hardest, while steadier sectors such as utilities and household goods hold up better, though none escape unscathed.

Lessons from the 1970s and beyond and how Stagflation can be Dealt with

The definitive case study is the 1970s. In 1973, the Organisation of Arab Petroleum Exporting Countries imposed an oil embargo, causing oil prices to quadruple almost overnight. Energy costs surged, manufacturing slowed, and unemployment rose sharply. In the United States, inflation peaked above 12%, while GDP contracted and unemployment exceeded 9%. A second oil crisis in 1979, triggered by the Iranian Revolution, extended the stagflationary period into the early 1980s. The resolution came at significant cost: US Federal Reserve Chairman Paul Volcker raised interest rates to nearly 20%, successfully breaking inflation but triggering a severe recession before the economy recovered.

2021–2023 raised fears of a return to stagflation, as supply chain disruptions, energy price spikes, and aggressive fiscal stimulus contributed to elevated inflation alongside a fragile global recovery.

There is no easy solution. Conventional monetary policy is designed to address either inflation or unemployment, not at the same time. Economists generally agree that breaking stagflation requires tight monetary policy to anchor inflation expectations, supply-side reforms to boost productivity, fiscal discipline to restore confidence, and credible central bank communication. The key lesson from history is that delaying action makes the problem worse – in the 1970s, slow responses allowed inflation expectations to become entrenched, making the eventual correction much more painful.

Navigating the Storm: Asset Classes That Have Weathered It Best in the Past

Not all asset classes are affected equally in a period of stagflation. Historical data highlights several categories that have provided meaningful protection during period of stagflation.

Commodities have historically been among the strongest performers, as the supply shocks that cause stagflation tend to drive energy, agricultural, and industrial metal prices higher. Gold, in particular, is widely regarded as an inflation hedge and store of value.

Inflation-linked bonds (such as US TIPS or South African inflation-linked government bonds) provide returns that adjust with inflation, protecting the real value of capital even when prices are rising persistently.

Real assets such as property and infrastructure tend to hold their value better than financial assets during inflationary periods, though the benefit depends on the prevailing interest rate environment.

Value stocks and dividend-paying companies with strong cash flows and pricing power – particularly in energy, mining, healthcare, and consumer staples – have historically outperformed growth stocks during these periods.

As a general principle, diversification across multiple asset classes and geographies remains the most reliable defence against any economic environment, including stagflation. Portfolios need to be adjusted in times like this to ensure that the real value of wealth is maintained effectively.

Not All Countries Are Created Equal: A Look at Those at Most Risk

Stagflation does not affect all countries equally. Nations reliant on imported energy and food – across Sub-Saharan Africa, South Asia, and parts of Europe – are most vulnerable, as supply-side shocks feed directly into domestic economies with little buffer.

Fiscal flexibility is a key differentiator. Developed economies with credible central banks have far more room to manoeuvre than emerging markets burdened by high debt, weak currencies, and limited borrowing access. Countries such as Argentina, Turkey, and Nigeria have experienced stagflationary conditions precisely because high debt-to-GDP ratios, currency depreciation, and foreign-denominated borrowing create a toxic combination

South Africa occupies an uneasy middle ground. A credible central bank provides some insulation, but dependence on imported fuels, structural unemployment, constrained fiscal space, and logistical bottlenecks leave the economy exposed – underscoring the importance of thoughtful portfolio positioning and geographic diversification.

Could this time be Different?

Today's economy shares some uncomfortable similarities with the 1970s, but there are some important differences. The biggest is artificial intelligence (AI). In the 1970s, no new technology was capable of offsetting rising costs and slowing growth. Today, AI is already reshaping how businesses operate – cutting costs, improving efficiency, and enabling companies to produce more with fewer resources. This could help keep prices in check even when other forces are pushing them higher. However, AI brings its own challenges: building the necessary infrastructure is expensive, and there are real concerns that automation could eliminate jobs faster than new ones are created, which would make a difficult economic environment even worse.

There are other reasons this time may play out differently. Central banks are better equipped than they were fifty years ago, energy supplies are less reliant on any single source thanks to renewables and natural gas, and financial markets are better at absorbing shocks. None of this guarantees a better outcome, but it does mean policymakers today have more levers to pull than their 1970s counterparts ever did.

To Conclude

Stagflation is a rare economic condition that challenges our understanding of how economies function. It defies normal rules, frustrates policymakers, and tests even the most experienced investors. Although true stagflation is relatively uncommon, the factors that contribute to it (such as supply disruptions, excessive monetary stimulus, and geopolitical instability) are not absent in today’s world. Understanding its characteristics, historical occurrences, and strategies for navigating it is essential for anyone aiming to protect and grow their wealth over the long term.

We remain committed to ensuring our clients are well-positioned to navigate any economic environment. In uncertain times, a disciplined approach, broad diversification, and a long-term perspective remain the foundations of sound investing.

Market Update

US equity markets staged a dramatic recovery in April, posting their strongest monthly performance since the pandemic era. The S&P 500 surged 10.42%—its first close above 7200 – marking the best month since November 2020. The Nasdaq 100 gained 15.64%, its best month in 23 years. The Dow Jones rose 7.14%, its strongest month since November 2024. An announcement of ceasefire talks, and a robust first-quarter earnings season underpinned the rally. The Federal Reserve held rates steady at 3.50–3.75% in April in what was Chair Powell’s final FOMC meeting before the transition to incoming Chair Kevin Warsh. The meeting revealed dissension among the members, as three preferred guidance of a hawkish nature. This hawkish tone and the increasing cost of energy pushed the US 10-year bond rate up to 4.3%. The month also saw key inflation and unemployment figures released, with CPI rising to 3.3% year-on-year; the monthly increase of 0.9% was consensus estimate of 59,000, with the unemployment rate falling to 4.3%.

European equity markets also rallied in April, though gains were more measured. Both the pan-European Stoxx 600 and Germany's DAX notched their biggest monthly gains since January 2025, at 4.83% and 7.11% respectively, supported by improving risk sentiment and hopes of a resolution to the Middle East conflict. The UK's FTSE 100 advanced 1.99% for the month, underperforming the broader European market as its heavy resource weighting provided less of a tailwind amid volatile commodity prices. The oil shock continued to dominate the inflation narrative: revised eurozone data showed March inflation at 2.6%, above the initial estimate of 2.5%, as energy costs fed through to consumer prices. The European Central Bank held rates unchanged at its April meeting, balancing concerns over energy-driven inflation against weakening growth. President Trump's announcement of a 25% tariff on EU automobiles added fresh uncertainty late in the month, though the impact was tempered by the Supreme Court's earlier ruling striking down much of the IEEPA tariff framework.

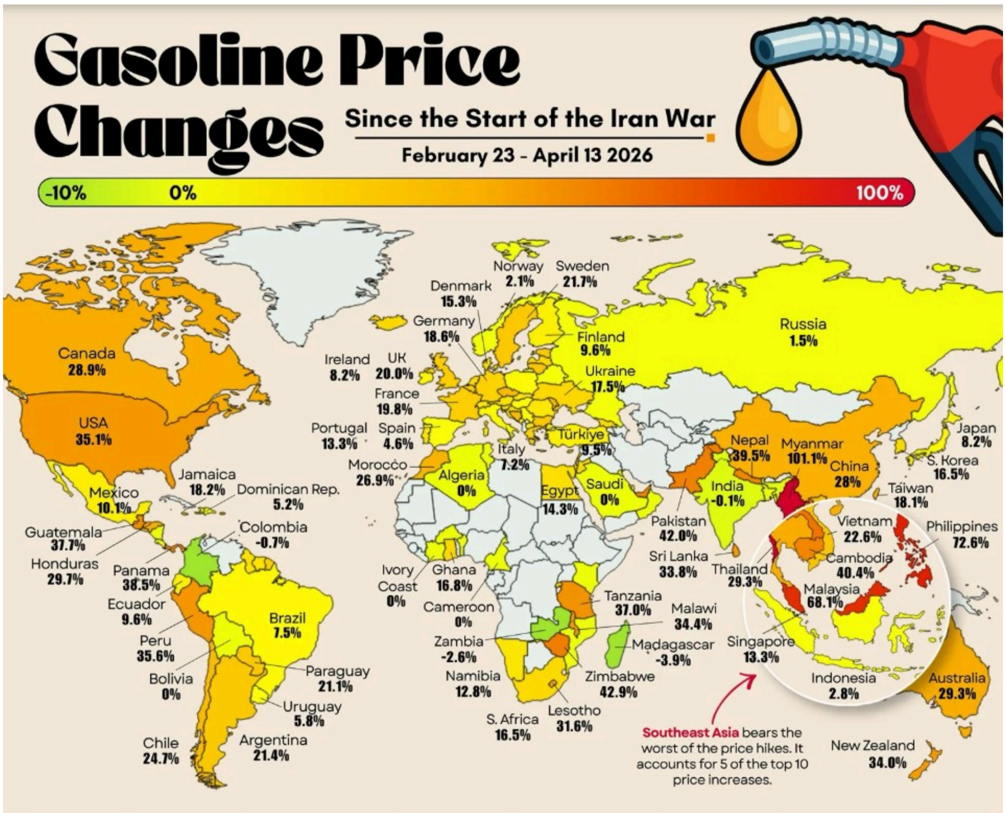
In Asia, Japan's Nikkei 225 surged approximately 16% in April, reclaiming and exceeding its pre-war record highs, supported by optimism around earnings and the Takaichi government's pro-growth agenda. China's Shanghai Composite climbed 5.54%, boosted by stronger-than-expected PMI data: the official manufacturing PMI came in at 50.3 in April, while the Caixin private survey reached 52.2, its highest level since December 2020. Hong Kong's Hang Seng advanced 3.99%, supported by resilient technology sector performance and improved sentiment around domestic demand.

Commodities remained volatile amid ongoing conflict dynamics. Brent crude experienced wide swings during the month, dipping to around $87 per barrel on 20 April as peace negotiations raised hopes of a ceasefire, before surging back above $115 as talks stalled and the US prepared for an extended blockade of Iran. Brent settled at $116 on 30 April, up 8.61% for the month, while WTI closed at $107, up 5.21% for the month. Gold traded near $4,600 per ounce on 30 April, slightly down 0.95% for the month, as the metal continued to consolidate following its sharp correction in March. Gold has declined approximately 13% since the commencement of hostilities in late February, with rising inflation and the prospect of higher interest rates weighing on the non-yielding asset.

Locally, the JSE experienced significant intra-month volatility. The Top 40 Index rallied sharply from its March close, reaching approximately 114,000 by mid-April as risk appetite returned. However, renewed US–Iran tensions and commodity price swings triggered a sharp pullback in the final week, with the index closing the month near 107,000—slightly up for the month at 0.88%. The rand strengthened against the dollar by 1.4%, due to dollar weakness against major currencies. March headline CPI edged up to 3.1% from 3.0% in February, in line with expectations, though the reading did not yet reflect the sharp fuel price increases introduced on 1 April. The SARB, which held the repo rate at 6.75% at its March meeting, raised its 2026 inflation forecast to 3.7% from 3.3% and now projects only one rate cut this year instead of two previously. Fuel inflation is expected to exceed 18% in the second quarter, posing a material upside risk to the near-term inflation trajectory. Despite these inflation concerns, the SA Government 10-year bond fell back to 8.9%.

Chart of the Month

(minimal or negative change) to deep red (very large increases). It highlights sharp spikes in parts of Southeast Asia, where markets such as Myanmar and Malaysia saw some of the steepest rises, alongside sizeable jumps in North America, much of Europe, and South Africa. Overall, it underscores the global nature of the fuel shock and the especially severe pressure on some emerging Asian economies.



“The four most dangerous words in investing are: ‘This time it’s different.’”
— Sir John Templeton

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