

moneywatch

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Investments

How diverse is your portfolio?

Investing for income is a long-established investment strategy.

First of all, it may be appropriate for those seeking to use a capital sum to generate an income from their investment. Others may choose to invest in specific funds which are designed to produce an income. It's also possible to reinvest the income, which could, over a number of years, make a significant contribution to the overall investment return.

Investors will generally look out for two types of investment, fixed interest funds or equity income funds which invest in stocks that have a track record of paying out dividends.

In the case of fixed interest funds, the funds invest in either government debt – known as gilts in the UK – or corporate bonds issued by companies to raise money on which they then pay a rate of interest.

In the case of equity income funds, a fund manager will identify firms that have a reliable track record of paying dividends. They tend to be more mature businesses usually in the mid cap or large cap sector.

The market globally has seen some interesting developments. For example, many emerging market

nations are offering inflation linked government bonds, while the number of companies globally that pay reliable dividends has been increasing. These developments have extended the investment universe significantly.

Of course, many fund managers see many opportunities in the UK in both corporate bonds and in income-producing shares, though recent problems at BP, which briefly suspended its dividend, may suggest investors need to consider how diversified their portfolio is.

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However, neither strategy is without risks. For example, the economic crisis means that government bonds are much riskier, particularly in Europe, while returns on all bonds are vulnerable to inflation.

Investment in equity is usually even higher on the risk scale.

If you have decided to focus on investing for income, you may consider investing in a new fund, perhaps with this year's Isa allowance.

Otherwise, if you have a larger portfolio, you might tilt your asset allocation. You may wish to move some interest-paying cash savings. Overall, cash deposits are safest with the least risk to both the capital sum and any desired income level, but that usually means returns are low and can be eroded by inflation.

If you are considering changing your investments to increase your income, please contact your IFA, who can help you match your attitude to risk to the appropriate investments.

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"Growing indications" that the worst of the downturn is behind us

Stock markets have had a better year to date, with some hoping the worst of this latest phase of the financial crisis will soon be behind us. Taking a range of assets, Merrill Lynch has noted that, in January, for the first time in two years, the price of shares, bonds, US treasuries, German bunds, gold and copper all advanced. Global equities in the MSCI AC World total return Index gained 5.6 per cent, its best January since 1997. The FTSE stood at 5,875 on Wednesday 8 February.

Most commentators pointed to an improving economy in the US and hopes that the Eurozone crisis is slowly stabilising.

"In January, for the first time in two years, the price of shares, bonds, US treasuries, German bunds, gold and copper all advanced"

In the UK, bank base rates remained at 0.5 per cent, inflation had fallen slightly with the Consumer Price Index at 4.2 per cent in December and the Retail Price Index at 4.8 per cent. Unemployment stood at 2.69 million or 8.4 per cent, the highest figure since 1994. Growth appeared to be faltering as the UK economy shrank 0.2 per cent in the last quarter of 2011, with some

fearing a double dip recession.

At least analysts believed it would not last long. Chris Williamson, the chief economist at economic research firm, Markit, said: "While the UK clearly faces a risk of sliding back into another recession, which is commonly defined as two consecutive quarters of declining GDP, there are growing indications that any downturn is likely to be mild and short-lived."

"Most commentators pointed to an improving economy in the US and hopes that the Eurozone crisis is slowly stabilising"

House prices rose in January up £844, according to the latest Halifax House Price Index. Prices rose to 0.6 per cent taking the average property value to £160,907 in January compared to £160,063 in December.

This same economic picture was broadly reflected in Europe, though there was better news for the US economy, which saw growth at 2.8 per cent in the last three months of 2011.

In terms of the eurozone crisis, the price Italy and Spain were having to pay to borrow from bond markets fell in January partly due to European Central Bank interventions, though the debate continued about the latest round of the Greek bailout, which was

unnerving bond markets again at the start of February.

On the company front, there was some good news for income investors. BP, posting annual profits of £15bn, increased its dividends by 14 per cent, bringing them to 5p a share. One merger on the cards in the UK was that of trading company Glencore and mining firm Xstrata, but the headlines were hogged by Facebook, which looked set to be valued at more than \$75 billion with around \$5bn shares due to go on public offer. However, Fund managers were uncertain whether it was worth investing at such a price.

For example, Sebastian Radcliffe, the manager of the £335m Jupiter North American Income fund, said he had concerns about how Facebook could monetise its user base.

"As Facebook begins to monetise its user base, there is little information one can gauge the extent to which this threatens to alienate core users," he told investment trade magazine Fundweb.

"In the UK, unemployment stood at 2.69 million or 8.4 per cent, the highest figure since 1994"

However, some fund managers were very bullish about markets in general. Julian Chillingworth, manager of the £60m Rathbone

"Investment is for the long term, and one of the most important things to get correct is your asset allocation, which is designed to help you deal with any short term fluctuations"

Blue Chip Income & Growth fund suggested that the FTSE 100 will breach 6,100 in the coming months.

Once again, we would stress that investment is for the long term, and one of the most important things to get correct is your asset allocation, which is designed to help you deal with any short term fluctuations. But, if you have any concerns about your portfolio, please contact us.

Points to remember

- The FTSE stood at 5,875 on 8 February
- UK bank base rates remained at 0.5 per cent
- In December the CPI was 4.2 per cent and the RPI was 4.8
- The UK economy shrank by 0.2 per cent in the last three months of 2011
- The US economy saw growth at 2.8 per cent in the last three months of 2011



Protection

New regulations could lead to price increase

Premiums on various types of insurance that come under the banner of protection insurance may rise by the end of this year. Some experts believe the premiums for new income protection, life insurance and critical illness insurance policies could rise. There are several reasons for this. First, new tax changes may make it more expensive for some insurers, those which also have an investment arm, to offer some types of protection insurance. A new European Union regulation designed to stop gender discrimination will mean that insurers have to offer the same rates to both men and women, but many experts argue this will increase prices for everyone, at least initially.

New international regulations about the amount of capital insurers have to hold, known as Solvency II, may also put up the price. All these developments may

see prices rise with some saying that premiums could increase by as much as 20 per cent. The very last thing we would advise you to do is to increase your protection simply because the price was going to go up later in the year. However, this may be a good time to consider your protection needs; what you have covered in terms of your income, your health and your life, taking factors such as an existing mortgage into account; and whether your existing insurance covers things

"This may be a good time to consider your protection needs"

that a new policy might not. So it may therefore make sense to keep your existing cover.

However, if you wish to take a look at the range of protection cover you have or are considering taking out more protection, please get in touch.

Introducing NEST; the UK's new workplace pension scheme

This year sees the introduction of major pension reforms in the UK, and a new workplace pension scheme called the National Employment Savings Trust, or NEST. The changes mean that employers will have to offer not just access to a pension scheme – something most are already legally obliged to do – but also offer contributions as well.

One of the features of the changes is the concept of “auto-enrolment”. Employees will be enrolled into their company pension scheme automatically and must actively decide if they do not want to join. Under current plans, employees will have to contribute 4 per cent of their salary, employers will contribute 3 per cent and the Government 1 per cent making a total of 8 per cent.

Eventually, this arrangement will cover all employers and employees, but it is being introduced for the largest employers first, with the contribution levels also phased in up to 2018.

The NEST system will begin in the next few months and will be fully in place in the next five or six years, as employers of different sizes start to accommodate the requirements. The Government has conceded some delays to small employers after they expressed concerns about costs, given the economic climate.

From 1 October this year, the biggest firms will need to accommodate the new



requirements. By February 2014, all firms with more than 250 employees must have adopted the new system. By 2017 all existing employers should have implemented the system, and by 2018 all employers, including new businesses set up after April 2012, should have done so. By 2018, employers of all sizes will be expected to be paying the full contribution rate of 3 per cent.

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Obviously, some employers already offer good company pension schemes. Those schemes should be assessed to see if they meet certain minimum standards which would exempt the employer from using the NEST scheme. The Government has created NEST

to manage the money for those employers who don't have a scheme in place already or where the existing scheme is deemed to be outside the NEST requirements. So there are, obviously, a host of financial planning issues to consider.

If you are an employer yourself, you will have to review your pension arrangement and contributions in the next few years, either by offering access to NEST or ensuring your

existing pension scheme meets the minimum standards. There are new duties as well. For example, it will be illegal for an employer to encourage employees to opt out of the auto-enrolment arrangements in order to save on the firm's contributions, and a system of

supervision is being devised to make sure this doesn't happen. If you have any concerns, please contact your adviser.

On a more positive note, employers may wish to consider how the new pension arrangements fit into their overall employee benefits strategy.

If you are an employee, and your employer currently does not offer any contributions, the new system is likely to be of benefit to you, because, provided you pay into your company scheme, your employer will have to do so as well at a minimum of 3 per cent, once the system is fully in place.

In other words, it will generally make sense to join because of the employer contributions on offer. However, if you have questions or concerns about the decision or indeed the pension and investment choices on offer, you may wish to consider taking individual advice as well.

If you are in a company pension scheme at the moment, there are fears that, faced with extra costs, some employers may make their existing pension scheme less generous, for example by cutting contributions back to the minimum 3 per cent.

In addition, some experts suggest that if you are investing the minimum of 8 per cent, it may not be enough to secure a comfortable retirement. This calculation may also change depending on your age.

For a host of reasons, we suggest that you check with your employer

what their plans are for the future and begin to consider what it may mean for you, particularly in light of your pension, saving and investing plans and your ultimate retirement goals. If, as an employee or an employer, you have any concerns about your pension arrangements or the forthcoming changes, get in touch for more information.

Points to remember

- From 1 October, the biggest firms need to meet NEST requirements
- By February 2014, all firms with more than 250 employees
- By 2017 all existing employers
- By 2018 all businesses set up after April 2012

RDR

Change to adviser charges

From the start of 2012, as part of the Retail Distribution Review, the way in which you are charged for and pay for independent financial advice will change. Until now, your adviser may have been paid by commission from a pension company or fund manager when the adviser recommended their product or fund. Your adviser will have used this commission as payment for the advice and services you have received and may have specifically offset any fee for those services against those commission payments.

Although all commission payments have had to be fully disclosed for many years, the regulator has continued to have concerns that the system risked biasing some recommendations. So, from January next year, pension providers and fund managers will be banned from paying commission. Advisers will

now be required to agree charges for the work they do and take payments under a new system known as adviser charging or customer agreed remuneration. They will still be able to take payment from the pension or fund, perhaps a certain amount upfront and then an on-going charge. This must be agreed with you. The product provider will have no role or influence in setting the level of the charges for advice though it may facilitate the payments. For ongoing advice and reviews, your adviser should provide you with a service level agreement, setting out what you are paying and the services you can expect for it.

In addition, some commission will continue to be paid on various insurance products, such as critical illness insurance, income protection insurance and life insurance, though as happens currently, your adviser will disclose this commission to you.

If you have any questions about this change and how it will affect you, please contact us.

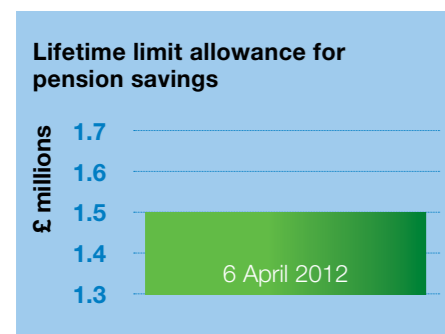
Planning for the new lifetime limit allowance

There have been several significant changes to the pension tax rules and other regulations in the last few years and allowances are much less generous. However, with careful planning you can maximise the amount you can save.

The lifetime limit

One significant change to pensions for higher earners is that the lifetime limit allowance for pension savings is due to decrease from £1.8m to £1.5m from 6 April 2012. Investors risk a tax charge of 55 per cent on money above the lifetime limit.

However, if you are aged over 55 or believe you have savings that could



reach the £1.5m limit soon, you can take action to mitigate the change, but you must act quickly.

You can, for example, apply for fixed protection. This allows a higher lifetime limit at the current level of £1.8m, but you cannot make any further contributions to your pension.

An alternative strategy may be to take money out of your pension now. This will free up some more of the lifetime limit. This could suit you if you wish to continue with pension contributions, but are also considering using pension drawdown in future. Money taken out before 5 April will use up less of a person's lifetime limit than that taken out after 6 April.

Pensions firm Skandia has calculated that if you take £600,000 from a pension fund before 6 April, this will mean only 33.3 per cent of your lifetime limit is utilised, compared to 40 per cent after 6 April. In monetary terms, Skandia calculates that this 6.67 per cent difference

Points to remember

- The lifetime limit for pension savings is due to decrease from £1.8m to £1.5m from 6 April 2012

“One significant change to pensions for higher earners is that the lifetime limit allowance for pension savings”

means an extra £100,000 of pension savings can be created without incurring a 55 per cent tax charge for exceeding the LTA of £1.5 million.

All strategies surrounding the lifetime limit require detailed planning, and we would urge you to contact your IFA as soon as possible. Time is of the essence, for example, if you wish to apply for fixed protection, an application must be made to HMRC by April 5 this year.

Two new bodies to replace Financial Services Authority

The Government has decided to shake up the regulatory system for financial services. It is abolishing the current overarching regulator, the Financial Services Authority and replacing it with two new organisations.

This is partly because the Government believes that what is known as the tripartite system of regulation where the Bank of England, the FSA and the Treasury policed the financial system including banks, did not perform effectively in the run up to the financial crisis. In particular, ministers feel that too many supervisory powers were taken away from the Bank of England.

The change with the most relevance to you as an investor will be the creation of the Financial Conduct Authority. It will regulate most financial companies, including supervising financial advisers and will have responsibility for introducing and policing new reforms in the advice market as part of the Retail Distribution Review.

One significant change is that this



new regulator will have the power to ban financial products for a year when it believes there is a significant risk of consumers suffering detriment because a product is deemed too risky and complicated.

The second body, the Prudential Regulatory Authority, will sit within the Bank of England with responsibility for making sure financial firms such as banks are sufficiently stable and have enough capital to ensure they do not pose a risk to the financial system. The Bank of England has

already created a new committee of financial experts, the Financial Policy Committee, which will aim to give an early warning of any other threats to the financial system.

The two bodies that consumers and investors are likely to have most contact with remain largely unchanged. The Financial Ombudsman Service will continue to adjudicate on unresolved complaints about financial firms and the Financial Services Compensation Scheme will continue to provide compensation in the event of the collapse of a financial firm.

Deadline approaching for this year's ISA allowance

Savers and investors have until 5 April to make use of this year's Individual Savings Account allowance. This year's allowance for a stocks and shares Isa is £10,680 with the amount having been made much more generous in the last few years. The Isa can be used to shelter your investments from taxes such as capital gains tax or income tax, and is a good way of disciplining

yourself to save and invest each year. The Isa regime also behaves in a different way to the pension regime. In broad terms, with Isa investment you are taxed before you put money in, but not when you take the income, while with a pension, your contributions are exempt when invested – i.e. you get tax relief, and you're taxed on the income you eventually take from it if it is sufficiently high.

Combined together, Isas and pensions can be very powerful tax and financial planning tools. There are a huge number of investment funds available to place in stocks and shares Isas with many different levels of risk. You can invest a lump sum or make regular payments though fund managers will set minimum limits. Your Isa allowance may also be utilised as part of your broader tax planning

and portfolio strategy.

You may also take out a cash Isa up to a limit this tax year of £5,340 and invest the other half of your allowance in a stocks and shares Isa. With a cash Isa we would suggest you make sure you secure as high a rate of interest as possible, though banks and building societies may offer a higher rate if you are prepared to limit your access to the money for

different periods of time, which is another factor to consider. You should check how it fits with other savings plans, including for example considering how much ready access to cash you need.

You may also wish to be more heavily invested in cash, given stock market volatility, but that is best considered as part of your overall investment portfolio strategy and we would still stress

the importance of still using your Isa limit. If you have any concerns, we would urge you to get in touch.

But one important thing to remember is that if you don't use this year's allowance, then you lose it permanently and it is best to give yourself some time to consider your decision rather than leaving it to the last moment.

Trusts still worthy

Despite Government changes, trusts should still be at the heart of any estate planning scheme

Trusts represent a very useful planning tool, in particular allowing you to pass assets on to your beneficiaries while potentially mitigating the impact of inheritance and other taxes.

The Government has, however, slowly tightened up the system in recent years and the tax treatment is less generous than in the past. However, trusts should still be at the heart of any estate planning strategy. They are not, unlike common perceptions, only for the very wealthy.

The trust is created when the settlor (the person who creates the trust) transfers assets to the trustees, who hold the assets in trust for the beneficiaries.

There are a host of reasons for setting up a trust. You may have a property in which you wish someone to retain a life interest, so they can live there before it passes to your beneficiaries or to allow one person to receive rent from a property but to leave the property to someone else on their death. You may wish to create a trust that pays income to several children, perhaps where you don't wish them to receive the assets in one go. You may wish to create a trust that leaves assets not just to existing but also to future grandchildren. You may wish to create a trust structure if you are part owner or owner of a business as part of business protection planning.

But the rules have become less generous. Apart from trusts for disabled beneficiaries, all discretionary trusts created on or after 22 March 2006 are likely to be

subject to IHT, at the time the trust is created and every ten years thereafter until the trust ends, and on assets leaving the trust. The exact amounts vary for instance, for smaller trusts it may be possible to use the nil rate band so that no IHT is payable when the trust is created.

Many trust beneficiaries were also hit by an income tax rise and capital gains tax rises in 2010.

But trusts can still help you manage the balance between capital gains, income tax and inheritance tax with the amounts you have to pay varying depending on the structures used. They can also help you with planning beyond more than one generation. They do involve



complicated financial planning and a consideration of any appropriate investment strategy as well.

It is also best to set up any trust structures with the help of both your solicitor and your IFA. Please contact us for further information.

Pensions

Boost your pension and keep your personal allowance

For those earning £100,000 or £150,000 and paying tax at 40 or 50 per cent respectively, the actual rate is more because, since the March 2011 budget, you are also losing some or all of your personal tax allowance. For every two pounds you earn over £100,000, you lose a pound of your personal allowance, losing it all when earnings equal £114,950. This significantly increases your effective tax bill and if you lose the full allowance you can pay extra tax of £2,990.

However, it is possible to mitigate the impact of this, i.e. to

potentially reduce your taxable earnings to below £100,000, thus retaining your personal allowance using several planning tools. These include tradable losses from a business, and grossed up gift aid, but arguably the most significant is to make extra pension contributions and to organise a salary exchange with your employer.

This can significantly increase your contributions to your pension, while allowing you to retain your personal allowance, but it requires a consideration of your finances overall. To look at how planning could help, please contact us.