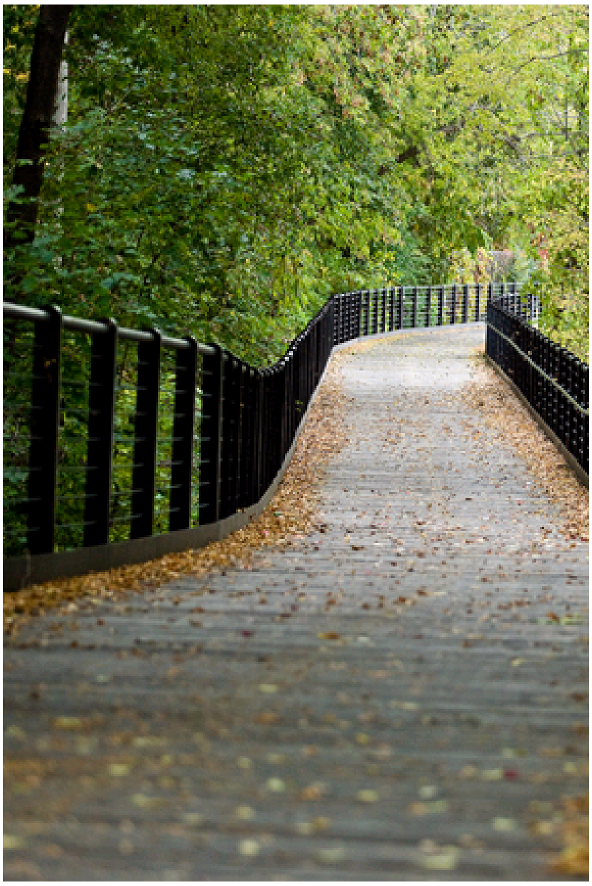
THE ADVISER.

Edition Seven ~ November 2009

Welcome to the latest edition of The Adviser, Kingfisher Independent Financial Planning's update on developments in the world of financial services.

The state of play



Amid signs that the recession is starting to moderate, the Confederation of British Industry (CBI) has raised its outlook for economic growth for the second half of 2009 and now expects Britain to have emerged from recession by the end of the year. Indeed, the Office of National Statistics revised economic growth figures up slightly for the second quarter of 2009, though the figures for Q3 have ended speculation that growth would resume by the end of September.

However, towards the end of 2009, the economy could benefit as consumers head to the shops ahead of VAT’s return to 17.5% on 1 January 2010. That benefit is likely to be short-lived as the shoppers will likely be those bringing forward purchases rather than being encouraged into something unplanned – which could then result in a fall in demand for 2010. Unemployment is also likely to hamper recovery; the CBI has forecast it will peak around three million. The CBI also expects the Bank of England to begin increasing interest rates sometime early in 2010, reducing households' spending power.

The CBI does, however, believes that economic expansion in 2010 is likely, albeit slow and fragile at only 0.1% and 0.3% for the first and second quarters respectively. The CBI commented, "The outlook is improving as the UK draws strength from quantitative easing, a weak pound and a recovering global economy," but went on to warn that, "conditions in the UK will remain tough for some time yet, and it is difficult to see where demand growth will come from."

Tips on surviving recession

NO 6: LOOK FOR QUALITY

During recessions and stock market downturns, high quality, established companies tend to fair better than their newer or more debt laden peers. A tough environment separates the wheat from the chaff as struggling companies are forced to cut their dividends and release negative trading statements. They will not be immune to the effects but quality stocks could help you through the worst of the storm. It is also worth noting that, if everything is falling, it could actually provide an opportunity to pick up more quality stocks at relatively cheap prices.

Contact Us:

Richard Salter IFA, , Kingfisher Independent Financial FP , Kingfisher House, , 19 Timbrell Street, , Trowbridge, , Wiltshire. , BA14 8PP (01225) 776652, , Info@kingfisherifa.co.uk

Professional Advisers

The annuity landscape

Thanks to the credit crunch, the landscape for annuity products has changed. Market volatility, low interest rates and changing investor demand have combined to bring new products onto market while others have fallen by the wayside.

Annuity rates are dependant on interest rates, so recent base rate cuts have hit prospective payouts quite hard. As a result, as investors have looked to tease out additional income, impaired life annuities and so called 'postcode annuities' have become more popular. Other potential retirees have simply decided to defer buying an annuity for as long as possible.

Market volatility has also affected the so-called 'third way' annuity products, originally designed to fill the gap between annuities and unsecured pensions, allowing exposure to the stockmarket, but with capital and income guarantees. They have had a difficult time as the cost of maintaining the guarantees has soared with the increased market volatility.

However, the market is also opening up to new ideas – for example, one new (fixed term) product is offering a secure rate of income for a pre-agreed term and then returning a guaranteed amount to the investor on maturity, which can then be rolled over into another annuity or income producing product. This ensures investors are not locked into what are currently considered very low rates for the long term and instead allows them a 'second chance' to get what might be better rates in a more favourable future environment.

Signs of life..?

The FTSE 100 Index has rebounded from the six-year depths of only months ago. The blue-chip index finally regained the psychologically important 5,000-point level in September, reaching its highest level for almost a year, and rallying by more than 40% since the March lows. Although it remains considerably below the levels reached before the demise of Lehman Brothers, there is concern that the UK equity market's rally has surpassed realistic prospects for corporate earnings.

Hopes of a burgeoning economic recovery in the UK and strengthening economic data from France, Germany and the US have provided investors with some encouragement. Corporate earnings from many companies have provided positive surprises, although it is worth remembering that some of these gains were achieved from cost-cutting and downgrading rather than through increased demand or higher turnover. The path ahead is unlikely to be trouble-free, and prospects for the UK stock market and economy remain far from clear. Looking ahead, if the economic backdrop does continue to improve, this is likely to provide further impetus for corporate earnings. However, if the early signs of economic revival begin to wane, then sentiment is likely to change rapidly from tentatively positive to negative.

On balance, the recent share-price rally is encouraging, not least because it demonstrates that UK investors are willing to go back into voltile equity investments. However, keep an eye out for news which might undermine investor sentiment.

New ISA limits

In the 2008 Budget, the Chancellor announced increases to the ISA investment limits. This has now been followed in the 2009 Budget by further increases to the limits, initially for the over 50s but eventually for everyone.

Under the new simplified rules, there are now just two types of ISA - the cash ISA and the stocks and shares ISA - and your overall allowance for both in 2009/10 is £7,200 - or, if you are over 50, from October, £10,200. Within this, the limit for cash ISAs - or for the cash element within a stocks and shares ISA - is £3,600 (or £5,100 for over 50s). But there is also some flexibility. You can, for example, now put the maximum £3,600 (£5,100) in a cash account and £3,600 (£5,100) in a stocks and shares account. Alternatively, if you place just £2,000 in cash, you can use the entire remaining balance - £5,200 (or £8,200) - to invest in stocks and shares. If you don't need cash at all, you can put your full allowance into stocks and shares.

You can also transfer any existing cash ISA holdings to a stocks and shares ISA without affecting your current tax year allowance. So, if you have £10,000 already sitting in existing cash ISA plans then this amount can be moved to a stocks and shares ISA whenever you think the time is right.

On 6 April 2010, the limit for everyone increases to £10,200 and the limit for cash within that goes up to £5,100. It might be time for all of us to start planning where we are going to put it.

What is critical illness cover?

Critical illness cover is a form of insurance protection which pays out a lump sum if you are diagnosed with one of a specific set of serious illnesses. The illnesses covered are the kind which will have a significant impact on your lifestyle or require it to change and, for example, generally include a heart attack, stroke and many forms of cancer.

The idea of critical illness is that it takes the financial stress away at a time when you might not be able to work for an extended period – or perhaps have to change job to one which pays less money. The plan pays you a lump sum and this can be used to perhaps reduce existing costs, such as your mortgage, finance changes which might be required to your home or even simply to go on an extended holiday to aid recuperation.

There are two types of critical illness policy – 'whole of life' and 'term' cover. As the names suggest, whole of life is designed to cover you for as long as you live whereas term is for a fixed period, usually 10 or 25 years and might be used to tie in with a fixed term liability such as your mortgage.

The conditions covered by critical illness cover remain a huge discussion point in the insurance sector as the small print does vary between providers. The Association of British Insurers (ABI) has moved to ensure some uniformity by publishing a list of 23 definitions of critical illnesses, but there are some insurers around who offer more than this.

As well as heart attacks and a stroke, the ABI list includes Alzheimer's, blindness, motor neurone disease and kidney failure. However, whilst this might seem straightforward, there are also several conditions which are excluded, or make a claim invalid – for example: drug abuse, Aids and, in some cases, contracting a terminal illness while living abroad. Some types of cancer may also not be covered – and it is therefore very important that you understand exactly what you are getting.

The other main issue to be aware of when buying a policy is whether your rates are guaranteed or reviewable rates. Guaranteed rates offer a set premium for the life of the policy whereas reviewable rates may be changed from time to time (usually annually) if the provider considers the risk levels they originally assumed have changed.

Sadly, cases do still crop up where the policyholder, having been diagnosed with a serious illness, discovers it is not covered by their policy. Robust, independent financial advice and a willingness to be open about your medical history are therefore a must when applying for cover.

Investing for income

Investors looking for a regular income stream often turn their initial thoughts towards corporate bonds and gilts or vehicles which invest in them. However, if you are prepared to take a long term view, the UK Equity Income sector can also offer solutions for income investors.

The Investment Management Association defines the UK Equity Income sector as comprising funds with at least 80% of their assets in UK equities, aiming for a yield in excess of 110% of the FTSE All Share Index yield (net of tax). These funds tend to concentrate on the income generation and therefore look just to maintain capital values - ie: rather than targeting actual capital growth as well. The main way of doing this is to invest in well established companies offering stable, growing dividends. More of these are found at the blue-chip end of the market and companies which are generating good cash flows, which means the funds can have a bias towards larger capitalisation stocks and those which are more established.

Historically, partly due to the tax regulations, the UK market has had a higher dividend yield than other markets, which accounts for the maturity of the equity income sector. However, the number of businesses in Europe awarding dividends is growing and even the US is beginning to follow suit – leading to the launch overseas income products as well.

Remember: the value of any market investment can fall as well as rise, but with equities - and particularly international ones - this risk is higher.

Pay off your mortgage early

One of the most effective ways to make savings on the interest on your mortgage is to pay it off early. Paying off the average 25-year loan can feel like a long haul but if you pay just a little bit more every month, it could save money in interest and might even cut years off the term of the loan.

However, there are a few things to consider. If you do not have a flexible mortgage, your lender might limit the amount you can repay before you incur charges. On the other hand, they might calculate interest annually – for example, if the calculation is based on the value at the end of December, then an overpayment in March will not take effect for nine months. In these circumstances, you might be better off leaving your money in a savings account for those nine months to earn a little interest first. Alternatively, if your lender does not actually allow overpayments, you might be able to reduce the term instead, which would increase your monthly payment, achieving the same result. However, this would be a permanent change so make sure you are happy to keep the higher payments going for the long term – and watch out for any hidden fees.

Alternatively, if you are happy with your mortgage or are still benefiting from a discounted or fixed-rate deal, put your spare money in a savings account and build up a lump sum instead. Alternatively, if savings rates are low, you could consider a remortgage. Another lender might offer a better deal, and some might even help towards legal costs.

Interest rate rises

Increases in interest rates don't just affect individuals, they affect companies as well. First, more profit is needed to pay higher debt charges - which could ultimately hit the share price. The price of corporate bonds will also be affected. As interest rates go up, the price of bonds goes down - because interest payments on bonds tend to be fixed, and rises mean these fixed payments become less attractive compared with other bonds or cash. All these issues can have an effect on the performance of your portfolio. However, if you have taken a long-term view, and your objectives are unchanged, the short-term ups and downs should be no real cause for concern.