THE ADVISER.

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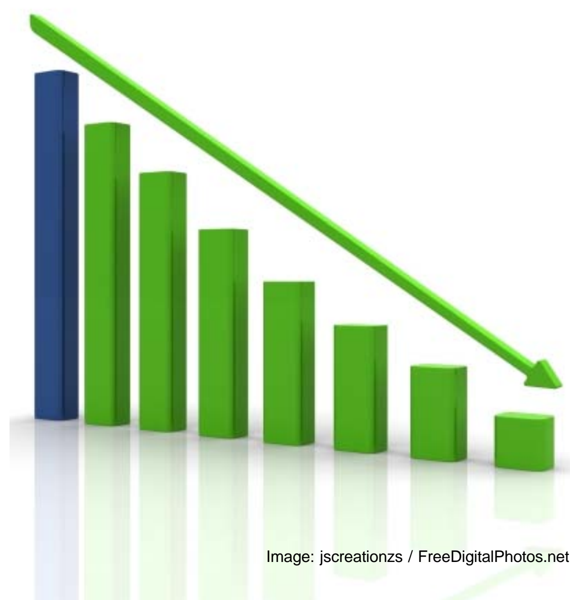
Welcome to the latest edition of The Adviser, Kingfisher Independent Financial Planning's update on developments in the world of financial services. In these unprecedented times of credit crunch and coalition Government, we have selected a range of articles which we hope will interest and inform you and would welcome your feedback on any of the topics covered or anything you would like to see included.

Planning for a market downturn

As an investor, you understand that different asset classes and industry sectors are liable to turn against you from time to time. Despite equities' long-term potential, both the meltdown of the 'dot.com' boom and, more recently, the credit crunch fallout demonstrate things are much less certain in the short term. Similarly, bonds are viewed as medium to lower-risk investments, particularly when economic growth is on the wane. However, holders of some bonds over the period since the crunch first hit would have suffered.



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Many investors, faced with such downturns, tend to panic. They see only the short-term loss on their portfolio balance sheet and forget their reasons for investing. Sadly, this is the worst thing they can do – and it is why planning at the outset of any investment is worth every minute spent. If you know why you are investing and understand fully the risks involved, market downturns should never have such an impact. If you are far-sighted and have a degree of nerve, they can even be an opportunity. Such downturns can be wide-ranging and indiscriminate, meaning the share prices of high-quality companies can suffer alongside lower-quality peers.

This gives canny investors the opportunity to add to their portfolio at bargain prices. However, for most, the best strategy is simply to protect yourself while the market settles down. Nothing in a portfolio is more valuable than the time you spend achieving balance, diversification and cementing that long-term objective.

What does it mean?

What does our new coalition Government mean for your financial plans? The UK economy is running an unprecedented deficit so we always knew that somewhere, one or two taxes will rise. In the spirit of compromise, there has been no imminent rise in the Inheritance Tax threshold and the priority instead appears to be an increase in personal income tax allowances instead. Alongside, however, the Chancellor has increased the rate of Capital Gains Tax for higher rate tax payers and given notice of a rise in Value Added Tax from next year. This comes alongside some significant cuts in public spedning, the full details of which are only just emerging. Now may be a good time to start a review of your own plans to make sure they can adapt.

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Paying off your mortgage

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 extra every month, it can save money in interest and might cut years off the term.
If you are in a position to over pay, there are a few things to look at first. A flexible mortgage is great as it will allow you to just pay extra whenever you can. If you do not have a flexible mortgage, though, your lender might limit the amount you can repay before you incur charges. In addition, they might calculate interest annually – ie: if it is only recalculated, say, at the end of December, then an overpayment in March will not actually reduce your interest payments for nine months. In this case, you might be better off putting money in a savings account to earn a little interest whilst you wait. However, even if your lender does not allow overpayments, you achieve the same result by reducing your loan term instead, which would increase your monthly payment. This would be a permanent change, though, so make sure you are can keep the higher payments going – and watch out for any hidden fees.

Finally, if you are happy with your mortgage or are benefiting from a special discount, you could just put your spare money in a savings account and build up a lump sum instead. Once the deal ends, you could then consider a remortgage to something more flexible, allowing you to achieve your aim another way.

YOUR HOME MAY BE REPOSSESSED IF YOU DO NOT KEEP UP REPAYMENTS ON YOUR MORTGAGE.

Covering your income

Income protection is an insurance policy that provides you with an income if you are unable to work as a result of accident or illness. Most policies will then pay a regular monthly amount until you have made a full recovery, until retirement age, for a fixed term - or death if earlier.

Income protection can be useful as a supplement to state benefits, as these generally prove insufficient to maintain the lifestyle you are able to enjoy on your current earnings. It is traditionally used to cover your salary and the maximum amount you can insure for will enable you to broadly match the after-tax earnings you would otherwise lose.

Costs vary depending on your circumstances, your medical history, the time for which you defer payments but also on the provider. The more you are covered for, the higher the premium. However, cheaper is not necessarily better and therefore, as with all forms of insurance and protection, it is imperative you read the small print on your income protection policy to ensure you know what is covered.

Finally, it is also essential that you are open about any previous medical conditions, regardless of whether or not you think they are significant. Non-disclosure remains one of the most common reasons for claims being declined by providers and will probably only arise right at the moment you most need the money. Financial advice is therefore highly recommended to help ensure you find the plan most suitable for you.

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Get in early

You only receive one ISA allowance every tax year. Since you cannot carry your allowance over to next year, if you do not use it, come the end of the tax year, you will lose it.

The annual allowance has been raised for everyone this tax year, to £10,200 (2010/11), up to £5,100 can be placed in cash - and this is available to be used any time up until 5 April 2011. However, you don't have to wait. You can invest any time from now and, particularly with cash ISAs, you might benefit more from doing so. The earlier you get your money into a deposit account, the more interest you will earn. For stocks and shares ISAs, there are those who try to 'time' their investment - that is, buy when prices appear cheaper (and thereby benefit more as they recover). However, even experts seldom manage to time the market on a consistent basis, and individuals can find it even more difficult. If you are concerned about market volatility, a better idea than 'timing' might be to drip feed your money in on perhaps a monthly basis - in other words, invest smaller regular amounts - to smooth out the risk of a price fall by buying your investment at a range of different price levels. This system is called 'pound cost averaging' and can offer long-term benefits, particularly for nervous, first-time investors.

Regardless of how you invest your money, however, remember you only receive one allowance a year. It is therefore best to start your research early and speak to your adviser about all the options. This will help ensure you make the right decision.

Taxation changes

Chancellor George Osborne has made it clear more than three-quarters of his deficit reduction proposals will stem from spending cuts. This still leaves some 25% of the deficit reduction to come from tax rises and these were outlined in the emergency Budget of 22 June. The biggest headline rise was in the VAT rate, from 17.5% to 20%. The Chancellor said he was focusing on spending – which is to some extent discretionary – rather than on higher income taxes, which are not.

As a result, income tax saw fewer changes. The personal allowance for under-65s was raised £1,000 to £7,475 but to pay for this, the basic rate tax band will be frozen until 2013/14. Notably, the Chancellor left some of his predecessor's measures untouched. Both the 50% tax band and the tapered reduction of the personal allowance for those earning more than £100,000 remain in place.

There were also changes to the National Insurance (NI) limits to bring them in line with the income tax bands. Based on current RPI forecasts, the lower limit will be reduced by £2,500 and the higher limit by £1,650. However, the previous Government's employee NI rises remain in place.

Prior to the Budget, much attention had been focused on capital gains tax (CGT). Rumours were rife of a rise to 40% or even 50% plus a reduction in the annual exemption but, in the event, none of this happened. Osborne raised the tax to 28% for higher-rate taxpayers and left the annual exemption at £10,100, which will continue to rise with inflation. Low and basic rate taxpayers will still pay the current rate of 18%.

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For the coalition's plans to be successful in avoiding a double-dip recession, the private sector needs to pick up the baton of growth from the public sector. The Chancellor therefore reduced corporation tax in a bid to improve the competitiveness of the UK as a place to do business. It will fall incrementally from 28% to 24% in four years' time, putting the UK in line with the European average of 25%.

Some issues remain up in the air. Osborne has ordered a review of the taxation of non-domiciled individuals and is also consulting with the pensions' industry on the reduction of pension reliefs proposed by the former administration. Stamp duty land tax for first-time buyers is also under review while more pain looks likely from the Comprehensive Spending Review this autumn.

Inflationary pressures rise

UK interest rates have now remained at their all-time low of 0.5% for over a year. The UK has crept tentatively out of recession but the new Government are now anxiously looking at ways to cut costs without doing anything to derail a very fragile recovery.

However, the UK Consumer Price Index reached 3.4% during March. In his open letter to the Chancellor of the Exchequer back in January, the Governor of the Bank of England (BoE), Mervyn King considered the rise to be a "temporary deviation" and suggested inflation will fall back below the Government-set target level of 2% in the second half of 2010. Even taking King's explanation for the sudden rise in prices into consideration, it is worth remembering the rate of inflation has almost doubled since November 2009. Indeed, only a few months ago, deflation seemed the more credible risk. In normal circumstances, the BoE would increase the cost of borrowing in order to cool inflation. However, rates are unlikely to rise in the short term because policymakers fear higher interest rates could endanger the UK's economic recovery.

Low interest rates are generally good news for borrowers, but are bad news for savers, who have already endured a year of exceptionally low interest rates. Returns on cash are meagre and high inflation is eroding the real value of cash. Looking ahead, Britons face the combined problems of high inflation and rising taxes, both of which will put additional – and unwelcome – pressure on disposable income.

Don't put off your will

It is understandable that so many of us put off the task of making a will. Afterall, it makes us think about our mortality and consider things which we hope will never happen. However, without one, you might be surprised to find out how easy it is for your assets to be distributed in an undesirable way.

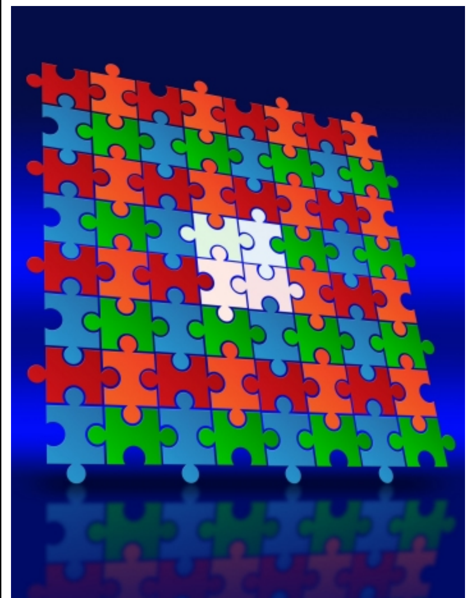
The exact rules of distribution depend where in the British Isles you live as some details differ between Scotland, Ireland and England & Wales. However, if you are not married, for example, the law is united in saying your partner may get nothing. Without a marriage certificate, your children and parents will benefit instead.

Even if you are married, there are many good reasons for making a will. First and foremost, it allows you to take postive decisions over who gets what - including friends, friends' children, charities and local societies who are entitled to nothing without your say. You can also decide if ex-partners - or perhaps more importantly, ex-partner's children - should be helped out. And, if your estate is greater than £325,000 (£650,000 for married couples), a will can help you plan to reduce your Inheritance Tax liabilities.

In thinking like this, making a will can actually become a very positive, rather than negative experience. Considering these things in advance can actually help your peace of mind and ensure that all you family and friends will be looked after in exactly the way you want them to be.

Planning for success

Step No 4. BE SMART
Benjamin Franklin's belief that "by failing to prepare, you are preparing to fail" might be something of a cliché in the twenty-first century, but it is worth thinking about before you begin the financial planning process. Not only do you need to make your objectives clear, you can also make them SMART. This is business speak for making sure you are Specific about what you are trying to achieve, can Measure the success (or failure) to keep your plans on track, keep them both Attainable and Realistic given your own circumstances, and that in the end, you will see something Tangible in return for the work you have put in.



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