INSIGHT

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WELCOME

Welcome to our latest issue of *Insight* from Armstrong Watson. Robert Kiyosaki, the American businessman and author of the best-selling book *Rich Dad, Poor Dad*, once remarked, 'Making money is common sense. It's not rocket science. But unfortunately, when it comes to money, common sense is uncommon.' As we continue into 2019, we look to de-mystify the ever-changing landscape of the financial world.

Spring is finally upon us, and those winter months are starting to become a distant memory. But with spring comes a new tax year. It may be tempting to leave the family finances ticking along. However, while you may feel the urge to give your home a spring-clean as we move into this time of year, why not take the same approach with your finances? On page 04, we provide some simple tips on how you can take a closer look at what you're spending as a family and help make significant savings.

Unforeseen life events and circumstances can potentially impact your finances in a number of ways. Believe it or not, you have an estate. In fact, nearly everyone does. Your estate is comprised of everything you own – your car, home, savings accounts, investments, life insurance, furniture, personal possessions – the list goes on. No matter how large or how modest, everyone has an estate and therefore shares something in common – you can't take it with you when you die. When that happens, you probably want to control how these things are given to the people or organisations you care most about, and we look into this further on page 15.

The full list of the articles featured in this issue appears opposite, and we hope you enjoy this Spring issue of our magazine. If you would prefer to download a digital copy or subscribe to new issues electronically, please visit https://www.armstrongwatson.co.uk/financial-planning-wealth-management.

Paul Dickson
Managing Partner

SPRING INTO ACTION

Taking a closer look at what you're spending as a family can help make significant savings

SPRING IS FINALLY UPON US, AND THOSE WINTER MONTHS (EVEN THOUGH WE'VE HAD A REALLY MILD WINTER) ARE STARTING TO BECOME A DISTANT MEMORY. BUT WITH SPRING COMES A NEW TAX YEAR. IT MAY BE TEMPTING TO LEAVE THE FAMILY FINANCES TICKING ALONG. HOWEVER, WHILE YOU MAY FEEL THE URGE TO GIVE YOUR HOME A SPRING-CLEAN AS WE MOVE INTO THIS TIME OF YEAR, WHY NOT TAKE THE SAME APPROACH WITH YOUR FINANCES?

Here are some simple tips on how you can take a closer look at what you're spending as a family and help make significant savings.

CREATE A BUDGET AND TRY TO STICK TO IT

The best financial planning begins with a piece of paper and a pen (okay, you may want to use a computer and spreadsheet). By working out your family incomings alongside your outgoings, you'll soon spot easy ways for saving cash, such as cutting down on takeaways or shopping trips for a single item.

If you're looking to track your finances more closely, you could use an app to help keep on top of your income and expenditure budget. This will instantly show you how much money is spare so you don't overstretch yourself.

CLEAR LOANS OR CREDIT CARDS WITH SAVINGS

If you're just clearing the minimum payment on loans and credit cards despite having cash in the bank, then it's worth doing the maths to work out what's actually doing more for you. Your savings could be earning little or no interest, while your payments are costing you money in interest.

While it's good to keep a nest egg for an emergency, in this scenario you're paying for the privilege of doing so – money that would be better spent elsewhere.

TAKE A LOOK AT YOUR CREDIT REPORT

Whether you want to take out new lines of credit or not, it pays to stay on top of your personal financial data. In the UK, the three

IF YOU'RE JUST CLEARING THE MINIMUM PAYMENT ON LOANS AND CREDIT CARDS DESPITE HAVING CASH IN THE BANK, THEN IT'S WORTH DOING THE MATHS TO WORK OUT WHAT'S ACTUALLY DOING MORE FOR YOU.

main credit reference agencies (CRAs) are Experian, Equifax and Callcredit. Be aware that repeatedly applying for credit can harm your chances of getting credit, because lots of credit searches might indicate you're having problems. You can apply for your credit record as often as you like, though.

REVIEW YOUR INSURANCE COVER

Being underinsured or overinsured will cost you money either way. Whether it's life insurance, policies for your home, car, medical bills or travel, or just a backup in case products break down, put a date reminder in your diary a month before the renewal. You'll then have enough time to shop around and ensure you get the best possible quote for your specific needs.

DON'T FORGET ABOUT YOUR PENSION POT

For many people, retirement may feel a long way off, but with UK life expectancy increasing it pays to think ahead. Many people choose to pay off their mortgage with surplus cash rather than invest in a pension. But for many, owning a home is still a dream.

Whether you're a millennial or nearing the end of your working life, you need to keep a constant eye on how much your pension is performing and whether it needs topping up. This is especially important with the latest changes to the State Pension age.

CHECK YOUR COUNCIL TAX BAND

Some homes are in the wrong Council Tax band, as houses in England and Scotland were put into valuation bands in the early 1990s – bands that don't accurately reflect what the house is worth today. You can check what band your property fits into on the Government's website and, if you feel the band is incorrect, challenge it as well.

USE THE INTERNET WISELY TO SAVE BIG

Online comparison sites are one quick way to save money, but consider using voucher code websites or buying online through sites where you can receive cashbacks on purchases from many top brands and stores, so you could soon see the savings mount up.

Also, don't forget to empty your browser's history and cache when shopping for the best deals. Some sites remember if you've already looked at a product and won't give you the best price, presuming you want the goods too much already – a tactic common among airlines and holiday websites.

GET YOUR CHILDREN INVOLVED IN SAVING

Teaching kids the value of money can instil the financial skills they'll need as an adult and even stop them from wanting you to spend so much. Set up jars around the home for them to put coins into instead of buying sweets or toys.

Visually seeing the coins mount up encourages them to save and skip impulse buys. You could even write a monetary goal on the jar to incentivise them further – either the amount to reach or what will be bought, whether it's a video game or a new bike. ■

John Hunt
Financial Planning Consultant, Dumfries

GETTING YOUR FAMILY FINANCES IN ORDER

These tips are just a few simple ways to spring-clean your finances – and there's no time like the present to start. Keep a list of what you save each day, and you'll soon be encouraged to save harder and faster as the amount grows. Please contact us to find out more about our services and how we could help you make the most of your hard-earned money.

DOUBLE WHAMMY

New social phenomenon – the 'sandwich generation'

IN RECENT YEARS, A GROWING REALISATION HAS FORMED THAT WE'RE IN THE MIDDLE OF A NEW SOCIAL PHENOMENON – THE 'SANDWICH GENERATION'. THE TERM 'SANDWICH GENERATION' IS OFTEN USED TO REFER TO THOSE WHO CARE FOR BOTH SICK, DISABLED OR OLDER RELATIVES AND DEPENDENT CHILDREN.

With an ageing population and many people starting families later in life, 'sandwich caring' responsibilities are on the rise. However, new research from the Office for National Statistics (ONS) has highlighted the fact that a pensions injustice could be making life even more difficult for this group.

TWIN RESPONSIBILITY

The report shows that almost 27% of sandwich carers show symptoms of mental ill health[1] while caring for both sick, disabled or older relatives and children. With life expectancy increasing[2] and women having their first child at an older age, around 3% of the UK general population[3] – equivalent to more than 1.3 million people – now have this twin responsibility.

Sandwich carers are more likely to experience symptoms of mental ill health – which can include anxiety and depression – than the general population (22%), according to the ONS analysis for 2016 to 2017[4].

The prevalence of mental ill health increases with the amount of care given. More than 33% of sandwich carers providing at least 20 hours of adult care per week report symptoms of mental ill health, compared with 23% of those providing fewer than five hours each week.

HEALTH SATISFACTION

People providing fewer than five hours of adult care each week report slightly higher levels of life and health satisfaction, relative to the general population. Some of the differences between the two groups could be explained by demographic differences. For

example, more than 72% of the sandwich generation are aged between 35 and 54 years, while 62% are women. Whereas among the general population, 38% are aged 35 to 54 years, and 51% are women.

Around 76% of those providing fewer than five hours of adult care say they're satisfied with life, while just 10% are dissatisfied. Meanwhile, 74% of the general population are satisfied with life, with 16% saying they're dissatisfied. However, when sandwich carers spend more than five hours a week providing adult care, they report lower levels of life and health satisfaction than the general population.

SANDWICH CARERS

Those providing between 10 and 19 hours of adult care per week are least satisfied according to both measures, even compared with those giving at least 20 hours each week. This could be because 69% of carers in the 10 to 19-hour category are in work (either employed or self-employed), compared with 41% of those providing at least 20 hours a week.

Similarly, many sandwich carers are not satisfied with the amount of leisure time they have. Those looking after their relatives in their own home – half of whom provide at least 20 hours of adult care per week – are least satisfied.

GENERAL POPULATION

Overall, around 61% of the general population are happy with their amount of leisure time, compared with 47% of sandwich carers looking after their relative outside the home and 38% of those providing care within their own home.

As well as reporting a lack of leisure time, 41% of sandwich carers looking after a relative within their home say they're unable to work at all or as much as they'd like. The ONS report also shows that women sandwich carers – who account for 68% of those providing at least 20 hours of adult care per week – are more likely to feel restricted than men. Around 46% of women feel unable to work at all or as much as they'd like, compared with 35% of men.

LABOUR MARKET

Women sandwich carers are also much more likely to be economically inactive than men – 28% are not part of the labour market, compared with just 10% of men in the same situation. It should be said, though, that the majority of sandwich carers are able to balance their job with caring responsibilities. More than 59% of those providing care at home say this does not prevent paid employment.

Clearly, caring for two generations could have an impact on carers' finances. One in three sandwich carers say they are 'just about getting by' financially, while one in ten are 'finding it difficult' or 'very difficult' to cope. Meanwhile, only 17% say they are 'living comfortably', compared with 32% of the general population. ■

Kerry Chaloner
Financial Planning Consultant, Northallerton

PREPARING FOR A MORE SECURE FINANCIAL FUTURE

As concern grows among sandwich carers, so too does the need to financially plan for ageing dynamics and family relationships. To discuss any concerns you may have, please contact us. We look forward to hearing from you.

Source data

[1] This is based on the General Health Questionnaire (GHQ), where a score of four or more indicates symptoms of mild to moderate mental illness such as anxiety or depression. The GHQ is self-reported.

[2] Life expectancy at birth in the UK did not improve in 2015 to 2017, having risen consistently for decades beforehand. The ONS investigated the stalling of improvements in life expectancy and its links to mortality rates.

[3] For the purposes of this article, the general population is all adults (including sandwich carers) aged 16 to 70 years.

[4] The ONS analysis defines sandwich carers as people aged 16 to 70 years who have a dependent child (one aged under 16 years, or 16 to 18 years, who is in school or non-advanced further education, not married and living with parent) in their home, and also provide regular service to a relative (usually parents, parents-in-law, grandparents, aunts or uncles, or another relative) who is 'sick, disabled or elderly whom you look after or give special help to'. The analysis is taken from Understanding Society, the UK Household Longitudinal Study. Households are surveyed each year either through a face-to-face interview or a self-completed online survey. Data collection takes place over a 24-month period, and the sample size for the general population in the 2016 to 2017 period was 34,000 individuals.

EVERYONE HAS THE SAME PENSION ALLOWANCES, DON'T THEY?

Incentivising people to save for their retirement

TO INCENTIVISE PEOPLE TO SAVE FOR THEIR RETIREMENT, THE GOVERNMENT PROVIDES BILLIONS OF POUNDS EACH YEAR IN PENSIONS TAX RELIEF, BUT TO AVOID THIS EXPENDITURE GETTING OUT OF CONTROL IT PLACES A CAP ON THE AMOUNT YOU CAN SAVE EACH YEAR AND UPON WHICH YOU CAN RECEIVE RELIEF. THIS CAP IS KNOWN AS THE 'ANNUAL ALLOWANCE'.

To compound the issue, the Annual Allowance has reduced significantly over recent years – from £255,000 in the 2010/11 tax year to just £40,000 from 2014/15 onwards. You need to have annual earnings to support this figure, so if you earn less than £40,000 your annual contribution limit will be correspondingly lower.

All taxpayers receive tax relief at the 20% basic rate. Those who pay tax at the higher (40%) or additional (45%) rates are able to claim the extra 20% or 25% via their tax return. Those residing in Scotland pay different rates of tax – 20%, 21% and 41% – but the rules for claiming tax relief remain the same.

If you haven't utilised your Annual Allowance every year, it is also possible to go back three years to make additional pension payments to carry forward unused contributions. You must have sufficient earnings in the current tax year to support the payment being made, though. Strict rules apply here, so it makes sense to contact a professional for guidance and advice.

TAPERED ANNUAL ALLOWANCE

If your earnings exceed £150,000, this can affect your Annual Allowance, and the Tapered Annual Allowance (TAA) will apply. Once this figure has been reached, income from all sources is taken into account – salary, dividends, rental income, interest and employer pension contributions – and for each £2 earned in excess of £150,000, your Annual Allowance will be reduced by £1. Once your income reaches £210,000, you will be left with an Annual Allowance of just £10,000.

Again, this is a complex area, so professional guidance and advice is recommended.

THE MONEY PURCHASE ANNUAL ALLOWANCE (MPAA)

The MPAA was introduced to limit contributions to £4,000 per annum for those who have flexibly accessed their defined contribution (DC) pensions. Situations when you'll trigger the MPAA are as follows:

- If you take your entire pension pot as a lump sum or start to take ad-hoc lump sums
- If you put your pension pot money into a flexi-access drawdown scheme and start to take an income
- If you buy an investment-linked or flexible annuity where your income could go down; and/or
- If you have a pre-April 2015 capped drawdown plan and start to take payments that exceed the cap (150% of Government Actuarial Department limits)

Before you consider taking any money out of a pension, you should seek professional advice, but there is also one more thing to consider with allowances and pensions – the Lifetime Allowance

The Lifetime Allowance is a limit on the amount of pension benefit that can be drawn from pension schemes – whether lump sums or retirement income – and that can be paid without triggering an extra tax charge. The Lifetime Allowance in the current tax year is £1,055,000 and should now increase in line with inflation each tax year.

If you are a high earner and paying in large contributions, or have been paying into a pension for a long time, you should check whether the value of your pension benefits is approaching, or above, the Lifetime Allowance. It may be necessary to consider taking your pension early or to stop contributing to the scheme, even though you have not retired, to avoid your benefits exceeding the Lifetime Allowance.

The test for the Lifetime Allowance is done each time you access a pension benefit. Each time you do so, you use up some of your Lifetime Allowance. There are 13 Benefit Crystallisation Events (BCEs), and it applies to both defined contribution schemes as well as Final Salary/Defined Benefit schemes.

Any pension savings above the Lifetime Allowance are subject to the Lifetime Allowance charge, which is currently:

- 55% if the excess is taken as a lump sum
- 25% if the excess is taken as income, plus Income Tax at your marginal rate

CAN YOU PROTECT AGAINST THE LIFETIME ALLOWANCE?

There have been many changes to the Lifetime Allowance. For the 2015/16 tax year, it was £1.25 million, but it was reduced to £1 million for the 2016/17 and 2017/18 tax years, and it increased for the 2018/19 tax year to £1.03 million.

If you have any form of protection against the Lifetime Allowance, you should seek professional advice to make sure it still applies and you don't receive an unexpected tax bill when you access your pension benefits.

Due to changes in legislation, people now have potentially different pension allowances. And because of the complexities involved, the value expert financial advice has perhaps never been greater. If you want to find out more about any of the above and whether they affect you, or to speak to us about any aspect of your retirement planning, please contact us at one of our 17 offices across the North of England and Scotland, or email HELP@armstrongwatson.co.uk ■

Amanda Heys
Financial Planning Consultant, Kendal

BREAKING UP IS HARD TO DO!

How much money will you will need to live on later in life?

DIVORCE IS UNDOUBTEDLY ONE OF THE MOST DIFFICULT SUBJECTS TO TALK ABOUT. WHEN RELATIONSHIPS COME TO AN END, THERE ARE SO MANY THINGS TO CONSIDER – CHILDREN, HOME AND SUPPORT ARE NATURALLY THE FIRST THINGS YOU WOULD FOCUS ON. IN FACT, WHEN YOU BEGIN THE PROCESS OF SEPARATING A SHARED LIFE, THE SHEER NUMBER OF THINGS TO DEAL WITH CAN SEEM VERY DAUNTING. AND THE COST OF DIVORCE CAN HAVE A LASTING IMPACT ON YOUR PLANS FOR LATER IN LIFE.

What is likely to be a divorcing couple's most valuable asset? The family home will spring to most people's minds first. But with the value of final salary pensions soaring, that forgotten 'defined benefit' income could well be the biggest single asset in the relationship.

A new study[1] has revealed that divorcees retiring this year can expect to receive up to 18% less in retirement income. While it may not be the first thing you need to think about, a pension fund is likely to be one of the most difficult assets a couple will have to split in the event of a divorce, so it's best to start early.

Average expected annual income:

- Never suffered a marriage breakup – £21,400
- Divorced – £17,600

That difference means that divorcees can expect to receive up to 18% less in retirement income.

Divorce can have a huge financial impact on people's lives. Many may not realise that the cost of divorce can last well into retirement, as divorcees expect retirement incomes of nearly £4,000 less each year than those who have never been divorced. And with the Office for National Statistics[2] confirming that divorce rates are increasing for men and women over 55, it is an issue likely to affect a growing number of the baby boomer generation.

The stress of getting through a divorce can mean people understandably focus on the immediate priorities like living arrangements and childcare, but a pension fund and income in retirement should also be a priority. Before planning how to separate your pension assets, you may want to consider how much money you think you will need to live on later in life.

SO WHAT ARE YOUR OPTIONS?

It's never easy when things come to an end, but support and advice can make the journey clearer. So what are the options available when you are ready to look at separating your assets?

Firstly, it is important that you both list the different pensions you and your ex-civil partner or spouse have. Then you can start to explore the options.

Across the UK, there are three core options to consider when you are separating pension assets:

- Pension sharing orders
- Pension attachment orders (called 'pension earmarking' in Scotland)
- Pension offsetting

Some of these options need to be administered by the courts, and not all of them will be suited to your individual circumstance.

PENSION SHARING ORDER

Pension sharing is one of the options available on divorce or the dissolution of a civil partnership. Each party owns a share of

the pension fund but is able to decide what to do with their share independently. This provides a clean break between parties, as the pension assets are split.

PENSION ATTACHMENT ORDER

This redirects some or all of the pension benefits to you or your ex-civil partner or spouse at the time of payment. When the person who owns the pension receives their benefits, the pension provider makes a payment to their ex-civil partner or spouse. With this option, you don't get the clean break as you would from the pension sharing order.

PENSION OFFSETTING

With pension offsetting, the total assets are considered and then divided up. For example, if your ex-partner has a large pension pot, they may decide to keep this, as you may agree to receive an asset of similar value (for example, the house).

Divorce can be a difficult and uncertain time, and the retirement you have planned may differ from the reality ahead. ■

Helen Tansley
Financial Planning Consultant, Leeds

Source data
[1] Research Plus conducted an independent online survey for Prudential between 29 November and 11 December 2017 among 9,896 non-retired UK adults aged 45+, including 1,000 planning to retire in 2018.
[2] Latest divorce statistics from the Office of National Statistics, published 18 October 2016

A PENSION IS A LONG-TERM INVESTMENT.

THE FUND VALUE MAY FLUCTUATE AND CAN GO DOWN, WHICH WOULD HAVE AN IMPACT ON THE LEVEL OF PENSION BENEFITS AVAILABLE.

PENSIONS ARE NOT NORMALLY ACCESSIBLE UNTIL AGE 55. YOUR PENSION INCOME COULD ALSO BE AFFECTED BY INTEREST RATES AT THE TIME YOU TAKE YOUR BENEFITS. THE TAX IMPLICATIONS OF PENSION WITHDRAWALS WILL BE BASED ON YOUR INDIVIDUAL CIRCUMSTANCES, TAX LEGISLATION AND REGULATION, WHICH ARE SUBJECT TO CHANGE IN THE FUTURE.

THE VALUE OF INVESTMENTS AND INCOME FROM THEM MAY GO DOWN. YOU MAY NOT GET BACK THE ORIGINAL AMOUNT INVESTED.

PAST PERFORMANCE IS NOT A RELIABLE INDICATOR OF FUTURE PERFORMANCE.

PENSION SHARING IS ONE OF THE OPTIONS AVAILABLE ON DIVORCE OR THE DISSOLUTION OF A CIVIL PARTNERSHIP.

AT THE MOST DIFFICULT OF TIMES, WE'RE HERE TO HELP

A pension fund is one of the most complex assets a couple will have to split, so anyone going through a divorce should seek legal and professional financial advice to help them do so. For many more couples, the increase in value of pensions means that it is often the largest asset. It goes without saying that this advice is crucial as early as possible in any separation where couples have joint assets. To find out how we can help, please contact us.

OUR GUIDE TO INVESTING

Giving you peace of mind and time to help you enjoy your life to the full

WITHIN THIS ARTICLE, I THOUGHT I WOULD SHARE SOME OF THE THINKING BEHIND THE WAY WE HELP OUR CLIENTS INVEST THEIR CAPITAL, AND HOW AND WHY WE HAVE PULLED THIS TOGETHER INTO A DOCUMENT CALLED 'OUR GUIDE TO INVESTING'.

Within our Financial Planning and Wealth Management business, the central commodity we deal in is advice. Our values and history drive us to build and develop long-term trusted relationships in order to ensure that we constantly deliver value to our clients, principally through providing advice to both individuals and businesses. A good proportion of this advice involves the investment of capital within a wide range of wrappers, such as pensions, ISAs and General Investment Accounts (GIAs).

PERSONAL OBJECTIVES

Every situation is different, of course, and clients' overall aims and objectives vary considerably, as do the stories behind where the capital came from. We take into account the clients' levels of knowledge and experience, as well as their personal objectives. Whether we are dealing with an investor with entrenched views (for example, those wanting to include ethical considerations within their approach, or preferring a passive rather than active fund management approach) or an inexperienced first-time investor with little investment knowledge who needs to be carefully guided through the experience, we work hard to really understand the level of support required at each stage of a client's life cycle.

We have recently developed and published Our Guide to Investing, and within this document we aim to convey both our investment philosophy and the main factors we believe are important, whatever your level of knowledge and experience.

SO WHAT ARE THE KEY FACTORS THAT WE BELIEVE SIT BEHIND ANY CAREFULLY PLANNED LONG-TERM INVESTMENT DECISION?

Risk – whatever one does with capital, there is risk in play. If funds are placed in a savings account, then the risk is inflationary. As time goes by, if the rate of return is lower than the rate of inflation, so the buying power of the funds will reduce.

Where funds are invested in real assets, then the risk is that the fund value can fall.

Through a combination of detailed conversations and a risk profile questionnaire, we understand the importance of ensuring that each client invests within their own comfort level to

best ensure that we minimise the chance of nasty surprises. The level of risk taken also needs to be regularly reviewed.

Diversification – it is unrealistic to believe that it is possible to consistently select the best performing asset classes and avoid the worst performing ones, so it makes sense that all the main asset classes are utilised, but in proportions that take account of the client's risk outlook. As well as asset classes, geographies and industries need to be diversified to maximise the chances of returns in line with expectations.

Time horizon – risk is proportional to time. The longer one's time frame, the more chance there is of meeting the investment objective. Downside volatility has the best chance of being overcome with a longer-term outlook.

Taxation – I cannot overemphasise the importance of sound tax planning to run alongside any investment planning. Using this approach, it is possible to generate a substantial retirement income and pay little or no Income Tax.

For example, we recently helped long-standing clients enter full retirement and worked for some years to equalise their pensions and build up a good-sized ISA portfolio alongside. This has enabled them to take £16,000 per annum each from their pension, where £4,000 is tax-free and the £12,000 sits within their personal allowance, so it attracts no Income Tax. They draw £5,000 each from their ISA portfolio, and overall this provides them with £3,500 per month with no tax liability whatsoever. When their State Pensions kick in, they will reduce their pension drawings and still only pay a small level of Income Tax.

PEACE OF MIND

Whether you are building up funds for the future, approaching retirement or considering how best to pass funds on to the next generation, it is important to review all of the above regularly.

We do this through cash flow forecasting, where we look at inflation, investment returns, life expectancy, income requirements now and in the future, and all sources of wealth and income, then produce a forecast, setting out to what extent your aspirations are realistic. This is repeated at each review to ensure that plans remain on track.

Our Guide to Investing hopefully articulates in simple terms how we support our clients through their own investment journeys, to achieve prosperity, a secure future and peace of mind.

To download your copy, please visit our website **www.armstrongwatson.co.uk**.

David Squire
Joint Managing Director

MARKET MOVEMENTS

What to expect

EXPECTATIONS VS REALITY

After several years of successful profits for mainstream markets, expectations going into 2018 were for continued global GDP growth and healthy corporate earnings. By year end, both of these had materialised. Cause for celebration? Not quite. Investment markets delivered negative returns in most areas. So, what happened?

ECONOMICS AND POLITICS – THE ODD COUPLE

Economic factors typically drive investment returns in the long term, but political events can be more dominant in the short term. As UK-based investors, the most obvious example of this is the continued uncertainty surrounding Brexit negotiations, and the impact this has had in discouraging corporate investment. From a global viewpoint, the biggest factor of 2018 was the trade war between the USA and China, with escalating tariffs causing concern for global growth rates. There was also Donald Trump's encroachment on the Federal Reserve, which perhaps encouraged the Fed's fourth interest rate rise as a statement of their independence. This not only upset Mr Trump, but also global markets. Add to this the attempted murder and murder of domestic dissidents in foreign lands allegedly by Russia and Saudi Arabia, and there were numerous political factors that contributed to the 2018 collapse of confidence in global stability.

UNDERSTAND THE PAST, EXPECT THE FUTURE

While these factors could just be considered an unlucky coincidence of (potentially) one-off events, it is perhaps more prudent to consider the likely range of outcomes investors should expect when putting their money to work.

WHAT IS NORMAL?

2018 saw losses across global markets, and this was especially the case in the UK, but it should be noted that market moves of this type are fairly common. One aspect of investment risk is measured through the volatility of historic performance. The 20-year average return of the FTSE 100 index is 4.39%[1], while the annualised volatility over this time period was 13.49%. This means that an annual return between +17.88% and -9.1% (4.39% +/-13.49%) should be accepted as a normal outcome (one standard deviation away from average). The FTSE 100 index fell by 8.73% over 2018 and, as such, is within this range.

TO FULFIL POTENTIAL, TOLERANCE IS NEEDED

As we progress through 2019, economic growth remains present (at the time of writing), and companies' earnings look set to increase. The drivers of 2018's losses appear to be receding, and valuations are at more attractive levels. The ingredients which may allow a stronger year are therefore in place, but, as ever, investors must accept that in targeting long-term returns, bumps in the road must be tolerated.

Richard Cole

CFA – Fund Manager - Future Money Ltd

Source data

[1] FE Analytics. 31.1.1999 – 31.1.2019

THE VALUE OF INVESTMENTS CAN FALL AS WELL AS RISE

INHERITANCE TAX

Beware the traps for the unwary

AS I HIGHLIGHTED IN MY PREVIOUS ARTICLE, THE GOVERNMENT'S TAX TAKE FROM INHERITANCE TAX (IHT) ALONE EXCEEDED £5.2 BILLION IN 2017/18, WHICH IS ALMOST DOUBLE WHAT IT WAS IN 2010/11. THE MAIN REASON FOR THIS INCREASE IS THAT SINCE 6 APRIL 2009, AN INDIVIDUAL'S IHT NIL-RATE BAND HAS BEEN FROZEN AT £325,000 WHILST ASSET VALUES CONTINUE TO GROW, WHICH MEANS A GREATER NUMBER OF ESTATES WILL BE SUBJECT TO IHT.

The introduction of the 'residence nil-rate band' on 6 April 2017 was intended to increase the reliefs available to estates, giving married couples and civil partners up to £1 million of relief when fully introduced. This should, therefore, ensure that HMRC's IHT take does not continue to increase as significantly as it has done so in the previous tax years. However, individuals should not assume that they will obtain this relief automatically because there are some traps for the unwary.

INCREASING RELIEF

The residence nil-rate band initially saw an additional £100,000 allowance being available to individuals against their family home or their previous family home if they had sold this previously and entered care. This relief is increasing from 2017/18 and is set to increase by £25,000 each year until 2020/21, when it will reach £175,000.

As with the IHT nil-rate band, the residence nil-rate band is also transferrable between spouses on death, and so by April 2020/21, spouses with estates valued at £1 million could be exempt from paying any IHT.

In order to benefit from the residence nil-rate band, there are a number of conditions which must be satisfied, including:

- The deceased must have owned a property
- The property must be (or was) used as the deceased's main residence
- The residence must be passed to a direct descendant such as children or grandchildren

This means people without children will not benefit from the relief, even if they pass their family home to their nearest family members. Furthermore, where a deceased's estate exceeds £2 million, the amount of residence nil-rate band is reduced by £1 of for every £2 it exceeds this amount. This might appear a high threshold, but if you own a business on death (which is exempt from IHT due to business reliefs), the value of this will be included when considering your overall estate value for the residence nil-rate band. As a result, we are seeing an increasing number of individuals lose this important relief because they are still a part of the family business. To ensure you qualify, you need to carefully consider when you should transfer your part of the family business to the next generation.

INSUFFICIENT PLANNING

The use of trusts within a deceased's Will is often recommended, particularly from an asset protection point of view. However, incorrectly set up, these can also affect the availability of the relief.

The increase in the Government's IHT take demonstrates that families are not planning ahead sufficiently to pass assets down to the next generation, but that can take a great deal of consideration, especially within a family business. However, for individuals with estates over £2 million, it is worth undertaking a review of your estate sooner rather than later to ensure that you maximise all your available reliefs for the benefit of your family. ■

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