money WISE

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Financial planning: get ready for 2016

2016 will see many changes that could affect your personal finances.

State pensions The new single-tier state pension will come in on 6 April. This will mean that the existing basic state pension and the various generations of additional state pension (including SERPS) will finish for those who have not reached State Pension Age (SPA). However, if you have reached SPA, you will be unaffected.

The initial level of the single-tier pension will be £151.25 a week (in 2015/16 terms), but this is not the whole story. Complex transitional measures mean that it is estimated that only 37% of those reaching SPA in 2016/17 will receive the full single-tier pension. By 2035 the proportion will have risen to 80%. Although the headline pension figure is much higher than the basic state pension (currently £115.95 a week), in the long term the new regime is forecast to cost the Exchequer less than today's state pension system, thanks to the disappearance of the earnings-related element. A corollary is that higher paid employees lose out under the single-tier pension while it improves the position of the lowest paid, who benefit least from today's State Second Pension (S2P).

Welfare benefits April will mark the start of a four year freeze on most working age benefits, including Employment & Support Allowance (ESA) which is paid if you are unable to work because of illness. 1 April is also the commencement date for a two stage reform of Support for Mortgage Interest (SMI). SMI meets interest costs (currently at 3.12%) on mortgages of up to £200,000 if you claim certain benefits (income-related ESA). At present SMI is payable following a 13 week waiting period after an appropriate benefit claim has started. From 1 April that period will revert to its pre-recession timescale of 39 weeks – a nine-month delay before any state assistance. Two years later the basis of the system will change from government payment to government loan. The interest-bearing SMI loan will then be repayable on your return to work or the eventual sale of the home.

Pension tax changes There are cuts to the two main pension tax allowances due on 6 April 2016, assuming that something more dramatic does not happen to the pension tax rules in the Autumn Statement on 25 November 2015. The lifetime allowance will be cut a third time, bringing it down to £1m. At current annuity rates that would buy a 65 year-old an inflation-proofed pension of no more than about £2,750 a month (before tax). The new rules for phasing down the annual allowance for high earners to a minimum of £10,000 will start at the same time. It will be possible to claim transitional protection from the lifetime allowance cut, but the final details will not emerge until after the reduction has occurred.

Please contact us now for advice on how these changes - plus the reforms to the taxation of dividends and interest – could affect you and the actions you should be considering before 2016 is well underway.

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How long does your pension have to last?

Pension flexibility means not having to buy an annuity, but how long will your pension fund have to last?

The Office for National Statistics (ONS) website has a calculator that estimates how long your pension will need to last (http://visual.ons.gov.uk/how-long-will-my-pension-need-to-last/). Enter your current age and gender and up will pop an estimate of your life expectancy. It may surprise you, along with some other information as you scroll down the page.

For example, for someone who is 50 years-old today, life expectancy is 86 years for a man and 89 years for a woman, but there is a 1 in 4 chance of the man living until age 95, the woman to age 98, and 12.3% chance of the man living to 100, 18.9% for the woman.

That data for a 50 year-old man can be reinterpreted as saying there is a one in four chance that his pension fund will have to last for at least 28 years rather than his life expectancy-based 19 years – almost half as long again.

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The flipside

The danger of running out of pension fund before you run out of life has a flip side: the risk that too cautious an approach leaves you running out of life before your pension fund expires. Given the favourable tax treatment of death benefits, this may seem a less important risk, but what it means is that you could have spent more in retirement and enjoyed a better standard of living rather than leaving a larger inheritance.

It is at this stage you may be wondering why nobody has invented a simple investment that is designed to last as long as you do, however long that is. In fact, the product does exist – an annuity. Perhaps that explains why at retirement some people are favouring a combination of fund withdrawals and an annuity, to give an element of life long income security. We are here to advise you.

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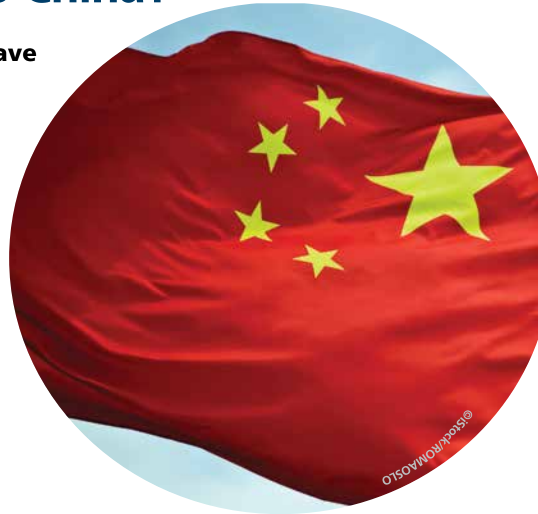
Just how important is China?

China's stock market and economy have dominated investment headlines recently. Is China *that* significant among emerging markets and what are the options for investments in China and the Far East?



China is the second largest economy in the world with a gross domestic product (GDP) at least three times that of the United States. However, the Chinese economy is now faltering and is dragging down the countries that depend on it with potentially worrying effects for international activity in general.

Bailing the rest of us out

As one economist has put it, for some years now China has bailed the rest of us out. It has taken the position of global consumer of last resort and has propped up slower growing economies through its demand for goods and services. However China has now itself slowed down and it's the emerging markets which will feel the brunt of this. Amongst the developed economies, Japan is most affected due to the nature of its close trade links to China, although as one of the world's leading exporters, Germany is not far behind.

Opportunities vs Volatilities

China is allowing greater foreign participation in its economy and becoming better integrated into the global financial system generally. This presents a wealth of opportunities for investors who are prepared to take a long-term time horizon.

At present, Chinese domestic retail investors dominate China's stock markets. This has created substantial volatility as they tend to react more strongly to market sentiment. China's heavy industry and state owned enterprises are a drag on Chinese and global activity, but to solely focus on them is to ignore the more dynamic service and property sectors which represent about two-thirds of activity.

The options for investment

Whilst there is a case for long-term investors to consider moving money to those regions at this time, it must be done carefully and possibly the best approach is to do so in stages. International research group Morningstar currently prefers funds from Fidelity, First State and Schroders in their portfolio selections for this region and Fidelity, JPMorgan and M&G for emerging markets generally. Those using portfolios or multi-manager funds may already have some exposure to these regions depending on the risk-rating being applied.

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New year cover review time

Do any changes to your circumstances in 2015 mean that your life and health cover needs adjusting? The first thing is to establish your stage of life.

Young, single with no children – life insurance may not be a high priority. Your biggest need will be to protect your income in the event that you suffer a disability. The premium rates are low and well worth investigating.

Young with partner and no children – life insurance is necessary to cover your mortgage and other debts plus a sum to give your spouse or partner time to readjust in the event of your death. It is easy to overestimate the cost of life insurance but income protection and critical illness are also necessary.

If you and your partner have chosen not to marry do not assume that the proceeds of any life insurance will automatically go to your partner. You will need to arrange third party cover or put a life insurance policy in trust.

Young with partner and children – your priority will be to provide sufficient life insurance cover to replace your income until your children are no longer dependent. There are special life insurance plans which pay a monthly income rather than a single lump sum which are ideal for this.

With partner and older children – apart from the types and levels of protection already mentioned, you should not overlook the fact that your spouse or partner will need to meet the cost of university education or perhaps even private school costs for your children. If you are self-employed you should make sure that you have sufficient additional life insurance to cover business debts and expenses.

Divorced or widowed – you should review any life insurance arranged earlier to make sure that it is still appropriate.

Post family/pre retirement – you may have elderly parents and at the same time your children may not yet be financially independent. Life and health insurance cover is more expensive but is just as necessary because of those who depend on you.

Retirement – the need for life insurance and health insurance (with the exception of private medical insurance) is diminishing at this stage of life. If you are concerned about inheritance tax (IHT) then you should investigate taking out a whole of life policy in trust. Many people in this age group will also be looking at funeral expenses. If you are concerned about your cover provision or IHT, you should seek advice.

Capital for kids

Tax rules changes are making it easier for parents to invest for their children.

If you make an investment for your own children, the taxman may be cautious. As a consequence, the tax rules say that if a parent gives money to their minor, unmarried child, then if the income generated in a tax year is more than £100, it is all treated as if it were the parent's.

Although every child has a personal allowance (£10,600 in 2015/16 and £11,000 next tax year), more than £100 of income (if capital is given by one parent and £200 if given by two parents) from parental capital could attract tax at up to 45%.

Gifts from grandparents, uncles, aunts or anyone else are not caught by the same treatment.

Three pieces of tax reform – one in force already – are resulting in the £100 tax trap becoming less of a problem:

- The £5,000 0% starting rate for savings income, which was introduced this tax year, can mean that if a child's interest income is assessed against a parent whose earnings and savings income are less than £15,500 a year, there is no tax to pay.
- In 2016/17 the new personal savings allowance will let every basic rate taxpayer receive up to £1,000 of interest, tax free and £500 of tax-free interest for every higher rate taxpayer, (additional rate taxpayers receive no allowance). So once again, interest income being assessed against you as a parent may still result in 0% tax.
- Next tax year will also see the introduction of the £5,000 dividend savings allowance for all taxpayers. This will mean that if you invest in share-based funds for your children and the dividends exceed £100, then tax will be nil until your dividend allowance is exhausted. Any dividends in the parents' own right will also be taken into account.

With the new tax year coming up ahead, now could be a good time for thinking about a present that could have lasting value.

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Stay calm in turbulent investment markets

Market volatility returned in August with more ups and downs expected if interest rates rise in the US and the UK. What should investors do? Here are some suggestions.

Look well ahead Research looking at the last 10 years has shown that if you had invested in the FTSE All Share Index for only one year you would have lost money in 20% of instances. However, if you had invested for 10 years, you would have lost money in fewer than 2% of instances.

Don't try to out-think the market It is really hard to get your investment timing right, especially in times of market turbulence. Sharp falls in stock markets tend to be concentrated in short periods of time. Similarly, the biggest gains are often clustered together. It is also quite common for a large gain to follow a big fall (or vice versa). If you try to anticipate when the best time is to invest you run a very high risk of missing the best gains.

Invest regularly Drip feeding money into the stock market can take away some of the worry of investing. If the stock market does continue to fall you will only have invested some of your capital. In addition, your future investments will take advantage of the cheaper share prices then on offer. Using annual ISA and pension allowances may encourage a certain amount of regular investment.

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