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Financial Health

Independent Financial Advice JUNE 2010

Why have the markets FALLEN?

The falls in the FTSE and in other markets around the world have pushed investment portfolios down after gains in the first part of the year. These falls happened for two reasons.

The first was the uncertainty caused by the election and the run up to the election. On virtually every occasion, stock markets have fallen before a UK general election. You will recall our previous advice to readers of this Update, to move out of UK equity investments. For those clients whose portfolios we manage, this meant a "tilting" of their portfolio so that UK (and European) investments were reduced and higher-risk investments in India, China and gold, for example, were increased together with lower-risk investments such as property, bonds and gilts. This movement helped to reduce losses significantly, which is just as important as achieving gains.

The second reason why stock markets have fallen is the impact globally of Greece, together with, more importantly, Germany's banning of "short selling".

The problems of Greece, as well as Spain, have been well noted in the media, and it would be understandable to think that this alone drove down the markets. However, it was the actions of Angela Merkel in Germany that caused a large part of the falls.

"Naked" or short selling is the process whereby traders sell assets that they don't already have! For example: if you believe that the value of, say, oranges (as a commodity that can be bought and sold) will fall from the present price of £3 to £2,

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you can sell them today at £3, with the intention of buying back what you have sold at £2!! I know it all seems strange and stupid, but there it is, and this is why the financial markets are such a strange place. With “short” selling, you can sell a currency that you don't have, before you buy it. IF you do this right, the sale that you have made, if you have sold enough, can virtually drive down the price because you have increased supply through your selling - this is what happened the last time the Conservatives were in power, when interest rates hit 15%!

In an attempt to stop all this, Merkel banned short selling. The effect of this was to cause people to panic sell. The massive increase of assets and currency hitting the markets caused their value to fall, hence the falls in stock markets around the world.

So what will happen now?

We believe the worst is over for the UK and the US, although we believe that Europe still has a way to go. Therefore, there should be a movement away from Europe and back into the UK. Also, moves made into higher-risk areas and lower-risk areas should now be reversed while UK stock markets are still low.

Action on capital gains tax

The emergency Budget scheduled for 22nd June will make changes to the CGT rules, which everyone expects will increase the taxation that CGT generates.

Presently, £10,100 in capital gains can be generated every year without incurring a tax charge. Any capital gain in excess of this is presently taxed at a rate of 18%. This present 18% rate was put in place by Mr Darling when he removed the tapering allowance, which itself had replaced indexation. Both indexation and tapering reduced the amount of CGT payable for people who held assets for a longer period of time. While this was a benefit for those holding assets, it was very difficult to calculate and so the removal of these allowances, and the reduction in CGT to 18% from the higher marginal rate, was seen all round as a sensible arrangement.

However, the Lib Dems have said that they want the CGT allowance to fall to £2,000, to help fund the increase in personal allowances to £10,000. This goes directly against the Conservative view of encouraging people to invest, as it penalises those who generate gains over time. It is for this reason that it is very hard to predict what the new government will do going forward. However, it is unlikely that there will be a reduction in CGT and so our advice would be to crystallize gains wherever you can. This means selling assets to "realise" the gain. This will generate a liability of 18% after allowances, but this is likely to be much lower than the expected taxation level.

Therefore, you should look into any assets that are easily realisable (shares, investment trusts, unit trusts, etc.), sell them, and, where appropriate, re-purchase them. This will realise the gain and crystallize the liability at the 18% level. One of the additional benefits of this is that the CGT liability will not be payable until January 2012.

Pension rules to change

It seems that hardly a month goes by without an announcement that pension rules are going to change. However, this month, the news looks pretty good.

The election of the new government means that some of their policies will actually be implemented. The biggest and most important of these is the annuity rules.

At the present time, when you reach age 75 you must either convert your pension to an annuity, or have an Alternatively Secured Pension (ASP). The problem with this is that an annuity usually dies with you, or if it is held jointly with your spouse, the income provided by the annuity will be significantly reduced. Under the new proposals, which we hope will be confirmed in the Budget, the compulsion to buy an annuity will be removed. This means that you can defer buying an annuity until you think the time is right. The consequence of this is that if you have not purchased an annuity, but retain the pension until death, the amount in the pension will pass down to the next generation, possibly free of inheritance tax.

The idea is excellent, but of course the devil will be in the detail. The other problem is that it is easy to say things in opposition, but it is a bigger issue when you are the government and must implement them. Why? Well, consider this.

If you don't have to buy an annuity, you can build up your pension over time with the express

intention of passing it down to the next generation. Presently, money held in a pension can pass to your children tax free. Therefore, how many people may simply increase the money in their pension, instead of in an ISA, for example, simply to shield them from inheritance tax which we know will not change a great deal in the new future.

This by-product of changing the rules is probably not something that the government had thought about, but will now be being considered in the run up to the Budget. Once the new rules are fully known, we will let you know how they may affect you and what you should do to take advantage of them.

New ISA Limits

From 6 April 2010, all ISA subscribers can contribute £10,200 into a Stocks and Shares ISA or £5,100 into a Cash ISA plus £5,100 into a Stocks and Shares ISA.

Best Savings Selection

To get the best from your deposit based savings you often need to move the money around. Use these rates to help you with your arrangements.

Top Three No Notice Accounts without Bonus

Name	Contact	£1 Gross %	£500 Gross %	£1,000 Gross %
Manchester BS	0161 9238015	n/a	n/a	2.66
West Bromwich BS	via branch	n/a	n/a	2.65
Stroud & Swindon BS	0845 7252423	n/a	n/a	2.25

Top Three Monthly Interest Accounts

Name	Contact	£1K Gross %	£2.5K Gross %	£5K Gross %
West Bromwich BS	www.westbrom.co.uk	2.96	2.96	2.96
Principality BS	0845 045 0452	2.86	2.86	2.86
n/a	n/a	n/a	n/a	n/a

Top Three Cash ISA's

Name	Contact	£1 Gross %	£500 Gross %	£1,000 Gross %
Nationwide BS	www.nationwide.co.uk	2.75	n/a	n/a
Newcastle BS	0845 605 0022	n/a	2.75	n/a
Nationwide BS	0800 302010	n/a	n/a	2.80

Please check with the terms and conditions before opening any account. If in doubt consult with your financial adviser directly as the above are for information only.

Child Trust Funds to be abolished

The Child Trust Fund was one of the flagships of the Labour government, and so it is hardly surprising that it is one of the first things to be hit by the cuts of the new government.

The CTF was introduced in 2005 to encourage parents to save for their children, and for some it worked, although the majority just took the government's money and said thank you very much.

From August, new parents will receive only a £50 voucher, with lower income families receiving £100. The payments previously planned for 7-year-olds will be abolished from January. Existing trust funds will continue, but no new money will be added by the government.

Should you do anything? On balance, not really. Those people who save for their children or grandchildren did so before the CTF, and will do the same after. The CTF will be consigned to having been a good idea that ultimately achieved nothing except giving a bunch of teenagers who were born at just the right time, a chunk of money to buy their first car.

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Ian is the owner and principal of Polestar, a trading style of Positive Solutions.

Ian has over 10 years experience in financial services and is qualified to an advanced level in taxation and trusts (G10) and Pensions (AF3).

He works principally with private clients addressing their concerns around inheritance tax, investment (for growth or income) and retirement planning. Ian also completes a significant amount of Continued Professional Development each year, attending various seminars and conferences, on his client's behalf, so that they are always kept abreast of latest developments.

"We are proud to be a small, focused firm, because this means that we provide higher levels of personal care and attention to detail. This is why many of our clients, who previously dealt with Banks and larger advisory firms, have come to us. Our clients want to be treated as individuals, not numbers, to have a closer working relationship and to have someone they trust be available to them at all times."

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