INVEST IN INFRASTRUCTURE
Diversify your portfolio with lesser-known funds

LIVING TO 100
Prepare for funding an extended retirement

INSIDE YOUR HEAD
How psychology affects investment decisions

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Ringing the changes of the new tax year

Starting 2019/20 as you mean to go on

In this issue...

Welcome to the spring edition of our newsletter, arriving just as we are looking ahead to uncertainty and change. The shift to the new tax year is one of the few certainties and our feature story reminds you of all the major tax changes for 2019/20. We also report on the retention of class 2 NICs boosting pensions for the self-employed and consider how tax relief changes are affecting landlords. For investments, we discuss potential diversification into energy and infrastructure funds. We also explore why you make certain investment decisions in our story on behavioural finance. All of which is even more important as longer life spans mean planning funding for lives that could span a century.

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INVESTMENT

Reap the rewards of regular savings

A regular savings plan is one of the most effective ways of building a nest-egg for the future.

Saving regularly can be a painless way to accumulate funds, particularly if you set up a direct debit to deduct this money on pay day. Set aside £100 a month, and you will have squirrelled away £1,200 after one year, or £6,000 over five years - and that's before counting any returns on investments. Trying to find a lump sum of this size to invest can prove more challenging, without getting a bonus, bequest or some other windfall.

COMPOUNDING THE ISSUE

The longer-term impact of regular savings should not be underestimated, as you can benefit from compound returns – that is getting investment returns on your investment returns. Over longer periods of time, compounding could significantly boost the value of your savings.

For example, a 5% return on a £1,000 investment gives you £50. With compound returns, if you leave that £50 invested along with the original £1,000 and get the same return, in the second year you could get £52.50, as you've earned 5% on £1,050. Over 10 or 20 years this effect can help snowball the value of your investments.

REGULAR INVESTMENTS

Those putting money into a stocks and shares ISA or other investment plan will find that regular saving helps smooth out the ups and downs of the stock market. There is an old investment adage that it is time in the market, not timing the market, that makes investors' money. With a regular investment plan you are not trying to second-guess market movements, so you don't run the risk of missing days when stock markets rise significantly.

Of course, this also means you will keep investing through market downturns. But if markets fall, you will be buying shares, or units in a fund, at cheaper prices. This means you could benefit as and when markets bounce back. The technical term for this is 'pound-cost averaging'.

Please let us know if you would like to discuss your savings strategies.

✢ The value of your investments, and the income from them, can go down as well as up and you may not get back the full amount you invested.

Past performance is not a reliable indicator of future performance.

Investing in shares should be regarded as a long-term investment and should fit in with your overall attitude to risk and financial circumstances.

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INVESTMENT

Building your assets with infrastructure funds

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Infrastructure funds are one of the less well-known types of investment, but they can offer options for those looking to diversify their portfolio

Infrastructure funds offer investors the opportunity to put their money into large physical assets, for example:

- Transport assets, such as bridges, toll roads, ports, airports and rail companies. This may include buildings as well as fleets of planes or trains.
- Energy assets, such as oil and gas storage facilities and transportation companies, electricity power stations and renewable energy projects.
- Other utilities, such as communication towers, satellites and water processing plants.
- Commercial property, including schools and hospitals, as well as commercial buildings like office blocks and leisure centres.

These funds provide access to investment markets that are not closely linked to the values of most other shares or bonds. So the value of these assets – and any income they generate – is less likely to be affected by the general ups and downs of the stock market.

It is worth holding a range of different types of funds to reduce risk. A serious correction in one sector or geographical region often has a severe knock-on effect on other equity markets. So, diversification across a mixed-asset portfolio can help offset the effects of such volatility.

Infrastructure funds can also be attractive if you're looking to generate an income from your investments. These types of assets can potentially earn reliable long-term income streams for investors – whether from fixed tariffs paid for generating green energy, or the tolls paid on roads and bridges.

Of course, like any investment, there is no guarantee that this income won't be reduced, or disappear altogether in certain circumstances if, for example, there was a cut in government backing for one of these infrastructure projects.

HOW TO INVEST IN INFRASTRUCTURE

In the past, most individual investors have found it difficult to invest in infrastructure. Direct investment into a power station can require large capital sums and has tended to be the preserve of professional investors and large pension schemes.

In recent years, however, a number of funds aimed at retail investors have been launched. These allow fund managers to pool investors' money to invest in this asset class. Some are UK-focused infrastructure funds, while others have a global remit. This is a niche area, and it is worth remembering that even large pension funds will only have a small proportion of their portfolio in such assets.

> *These investment markets are not closely linked to the values of most other shares or bonds.*

In addition to pension funds some multi-asset funds will also have exposure to infrastructure assets, and it is important to check the extent to which you might already be exposed to this sector through existing investments. You should not invest directly and only invest in regulated funds provided by some well-known investment providers.

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Investing in shares should be regarded as a long-term investment and should fit in with your overall attitude to risk and financial circumstances.

TAX

Ringing the changes of the new tax year

The tax year 2018/19 ends on Friday 5 April, which means it's time to start planning for the new tax year and tie up the loose ends of the old one.

Planning for the new tax year is now affected by the shift of the Budget schedule to autumn. The result is that changes announced in October, or in Scotland's December Budget, have now passed into legislation in time for the new tax year. So, what does 2019/20 hold in store?

A higher personal allowance

The first £12,500 of income for most people in the UK will be free of income tax from 6 April 2019.

An increased higher rate threshold, outside Scotland

The higher rate income tax threshold (the personal allowance + the basic rate band) will rise to £50,000 for England, Wales and Northern Ireland. This considerable jump of nearly 8% could mean it is worth reviewing how married couples and civil partners own their investments to ensure income falls into the right hands. In Scotland, the threshold stays unchanged at £43,430.

An increased national insurance contributions (NICs) upper threshold

The UK-wide upper threshold for full rate NICs (12% for employees) will also increase by nearly 8% to £50,000 from 6 April, potentially clawing back some, or in Scotland, almost all of your income tax savings. However, the increase does offer more scope to potentially gain benefits from salary sacrifice arrangements for pension contributions.

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Personal pensions
The lifetime allowance will rise by almost £25,000, to £1.055 million, for 2019/20 – roughly enough to buy a 65-year-old a guaranteed inflation-proofed income of around £34,000 a year, based on current annuity rates. The annual allowance and its associated taper limits remain unchanged. So it's all the more important to check whether you have any unused allowance from 2015/16 to carry forward before 6 April arrives, given you can only carry forward the previous three tax years, and the opportunity disappears.

Employer pensions
The minimum level of pension contributions for automatic enrolment increases from 6 April 2019. For employers, the minimum rate rises from 2% to 3% of 'band earnings' (£6,136–£50,000 in 2019/20), while employees must pay enough to bring the total up to 8% including tax relief. As the band's upper limit has risen in line with the NIC upper threshold, there is a double sting if you earn above £46,454.

The jump of nearly 8% could mean it is worth reviewing how married couples and civil partners own their investments to ensure income falls into the right hands.

Individual Savings Accounts (ISAs)
Only the Junior ISA investment limit will increase in 2019/20, and that by only £108 per year. It will be the third successive year the overall ISA limit has been fixed at £20,000, a reminder of the wisdom of contributing as much as you can each year (including 2018/19, if you have not already done so). One popular ISA variant, the Help-to-Buy ISA, will disappear for new investors (aged 16 upwards) from December 2019.

Capital gains tax (CGT)
The CGT annual exempt amount increases to £12,000 in 2019/20. The new annual exempt amount could result in a potential tax saving of up to £2,400 (£3,360 in the case of residential property). If you have not used your 2018/19 exemption, combining the two with sales straddling the tax years could remove £23,700 of gains from tax. That might provide the funds to top up ISAs and pensions.

For more information on any of these changes please contact us now.

✢ The value of tax reliefs depends on your individual circumstances.

Tax laws can change.

The Financial Conduct Authority does not regulate tax advice.

The value of your investment, and any income from it, can go down as well as up and you may not get back the full amount you invested.

For specific tax advice please refer to your tax specialist or accountant.

TAX

Self-employed pensions boost

The Chancellor has abandoned plans to abolish class 2 national insurance contributions (NICs).

Those registered as self-employed pay class 2 NICs if their profits are more than £6,365 a year in 2019/20. Then if profits exceed £8,632, they also have to pay class 4 NICs. Typically, these NICs are paid through the self-assessment system.

The planned abolition of class 2 NICs was proposed to simplify the tax system. But there were concerns it would push up pension costs for the self-employed, particularly those on lower incomes.

For 2019/20, the class 2 NIC is £3.00 a week. Class 4 NICs are 9% of their profits (between £8,632 and £50,000 for 2019/20) then 2% of profits above this level. Paying class 2 NICs gives the self-employed access to the new state pension, which is worth up to £168.60 a week in 2019/20 – depending on their NIC record.

But relying solely on the state pension in retirement isn't a sensible idea. It's important to make some private pension provision as well. You won't have the benefit of a workplace scheme or employer contributions – but that shouldn't stop you building up your own retirement savings.

Registered pensions are a really tax-efficient way to boost your income later in life.

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RETIREMENT

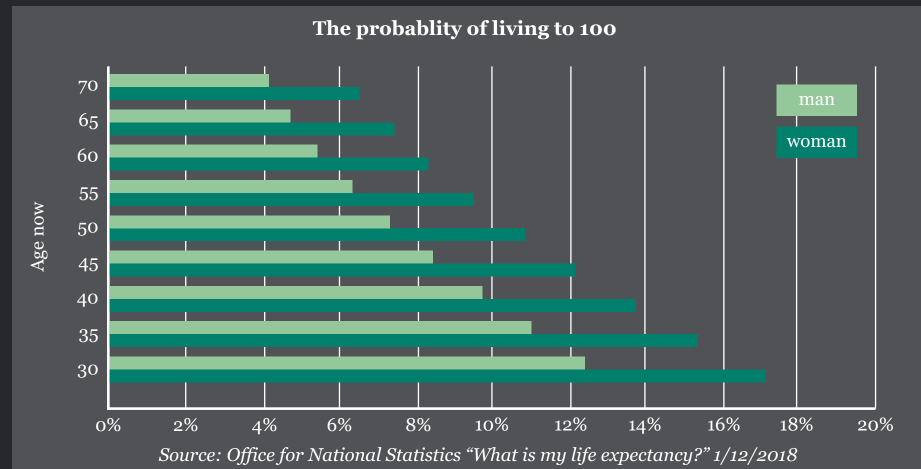
Planning for the 100-year life

Your chances of reaching 100 are probably greater than you imagine. It may sound fanciful, but a 100-year lifespan is well within the bounds of probability. That could have profound implications for your retirement planning.

While the average 70-year-old man now has a 4.1% chance of reaching his 100th birthday, an average 40-year-old woman has a nearly 13.8% chance of becoming 100. And the number of people who are likely to live well into their 90s has soared.

These Office for National Statistics data are based on the entire UK population, which means that they could well be an underestimate for you. There is evidence that life expectancy is affected by levels of wealth.

There are three big issues to look out for in planning a long retirement.



INCOME IN RETIREMENT

If you retire at 65 (and do not forget the state pension age will reach 66 by October 2020), then you could need your pension income to last for 35 years. The only way to guarantee your income for such a long period is to purchase an annuity. However, the price you pay will reflect the potentially long payment period and current low long-term interest rates. A simple fixed annuity for a single person starting at age 65 now, with no increases, will cost about £100,000 to produce an annual pension of about £5,500.

You could take income withdrawals from your pension fund and other investments, although that would not provide a throughout-life guarantee. Investment markets are almost bound to go through several cycles throughout your retirement. So your retirement fund would need careful management to handle the potential problems caused by drawing regular payments from it in falling markets.

INFLATION

Taking a fixed retirement income cannot be a long-term option because of inflation. The pound has lost over two-thirds of its value over the last 35 years as measured by the RPI. Even if inflation drops over the next 35 years, averaging just 2% annually, today's pound will be worth just 50p by 2054.

An inflation-proofed annuity for a single person costing £100,000 at age 65 would currently provide only a little over £3,200 a year.

FUNDING YOUR RETIREMENT

The minimum level of pension contributions for auto enrolment will be 8% of band earnings from 6 April 2019. Yet pension experts consider this will be nowhere near enough to fund a comfortable retirement for most people, even after allowing for a full state pension (£168.60 a week from April 2019).

There are plenty of suggestions for the appropriate level of savings to secure a comfortable retirement, but for a more accurate assessment, there is no substitute for the type of individual calculation we can offer, based on your personal circumstances.

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INVESTMENT

Keeping your head – the psychology of investment

Understanding your personal biases can help you form investment strategies that work for you across good times and when the going gets tougher.

Traditional finance theory starts from the principle that markets and their investors are perfectly rational. A quick look around will convince you that such an idea is optimistic to say the least. Rational markets would not fluctuate without any apparent reason, nor would rational investors feel the pain of a loss over twice as much as they enjoy the feel of equivalent gains.

The field of behavioural finance, which studies the impact of investor psychology on financial decisions, has developed in response to the inconsistencies between rational theory and irrational, human, reality.

Behavioural finance can offer lessons to all investors. People can act in surprising ways in all sorts of circumstances. For instance, you might ask yourself if you recognise any of these behavioural finance biases in yourself or others:

- **Overconfidence** Many people when asked identify themselves as 'above average', whether in terms of driving ability, intelligence or looks. By definition that cannot be true – no more than 50% can be above average. Overconfident investors can pay a high price to learn this truth.
- **Hindsight bias** How many times have you heard someone say "I always knew that was going to happen" after the event has happened? Yet the same person probably never warned you beforehand. People like to imagine their predictive powers are good – and some can convince themselves their hindsight was once foresight.
- **Herding** "Everybody is investing in technology/emerging markets/commercial property/etc., so I will too." It seems the easy option, not least because human beings are inherently fearful of going against the crowd. However, the crowd's judgement is not always right. Also, if and when the crowd changes its mind, the reversal can become a dangerous stampede, especially in investment markets.
- **Confirmation bias** Which do you pay more attention to, the information and comments that reinforce your views or those that contradict them? The natural response is the former, something that some people on social media have learned to exploit. However, when it comes to investment, hearing only what you want to hear could mean ignoring important if uncomfortable truths.
- **Self-attribution** You choose to invest in X and its value rises – that is proof of your skill. Then you choose to invest in Y and its value halves – that is just bad luck. Such a view of expertise makes us feel better about both outcomes, but it could be pure self-deception. It is also possible that the choice of X was down to luck and Y to lack of investment skill.

By developing an understanding of behavioural finance ideas, you can identify your own investment behaviours. The nearer you come to acting like a rational investor, the more you may be able to benefit from the irrationality of others.

A sensible starting point is to identify your innate biases and take advantage of the professional, objective advice we can offer when making investment decisions.

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TAX
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Landlords losing interest

The next step in changes to tax relief for landlords takes effect from 6 April 2019.

If you have a mortgage on a buy to let residential property, from this April only 25% of the interest can be offset against your rental income, with the remaining 75% qualifying for a 20% tax credit only.

For a higher rate taxpayer, that will mean £50 less tax relief for every £1,000 of interest in 2019/20. And from April 2020 onwards, you will only receive a 20% tax credit – another £50 cut in relief for every £1,000 of interest for 40% taxpayers.

If these changes make you think about selling up, then remember another April 2020 change: capital gains tax at up to 28% on residential property will be due within 30 days of sale.

✢ The value of tax reliefs depends on your individual circumstances.

Tax laws can change.

The Financial Conduct Authority does not regulate tax advice and some buy to let mortgages.

For specialist tax advice please refer to an accountant or tax specialist.

PROTECTION

Just in case: protecting against income cuts

You may assume you'll never need it, but if you experience redundancy or illness, you may become eligible for universal credit. However, if you imagined that the state would provide enough support in the event of financial difficulty due to sickness or unemployment, it's time to think again.

The government is rolling out universal credit, a new single payment system designed to replace six existing state benefits. Universal Credit is expected to be adopted nationwide by 2023. However, delays to implementation and complaints that the switch is leading to financial hardship have caused controversy.

Universal credit is paid monthly to those who are out of work, as well as to people in work but on low incomes. It replaces the following benefits:

- Child tax credit
- Housing benefit
- Income support
- Income-based jobseeker's allowance (JSA)
- Income-related employment and support allowance (ESA)
- Working tax credit

Relying on the state benefit system to provide an adequate safety net if you lose your job or you are too ill to work is generally unwise. It is designed to provide a basic standard of living and may not cover your mortgage or full rental payments. The amount paid under universal credit will depend on a range of factors, including your housing costs, number of children, other earnings or savings, and whether you have an existing disability.

GREATER PROTECTION

The good news is that insurance can bridge the gaps in your financial security if you lose your job, become too ill to work or die.

Term life insurance is the most basic type of life insurance. It pays out if the policyholder dies before a set date – usually retirement, or the end of a mortgage term. This is often a cost-effective option, because premiums are low as the chances of claiming are relatively low. However, should the worst happen, the lump sum can help ease financial worries at a difficult time.

Critical illness insurance pays a fixed lump sum payment if you are diagnosed with a specified serious illness, including most types of cancer, stroke and heart disease.

Income protection insurance pays a monthly amount – usually a fixed portion of your regular earnings – if you cannot work because of ill-health. This normally only pays out after you have stopped work for a certain period of time.

Such protection can cover your mortgage payments as well as other essential bills. All these policies can be purchased by individuals, but some employers also provide cover.

The government recently confirmed that any payment from these insurance policies won't affect your entitlement to state benefits such as universal credit. If you are concerned about potential consequences for your income if you fall ill, please get in touch.

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