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2015-16 ISAs COUNTDOWN TO THE END OF THE YEAR

As we approach the end of the 2015-2016 financial year, you still have time to make contributions up to the maximum allowable limit.

ISA type	Maximum contribution per person per year
CASH and/or STOCKS & SHARES ISA	£15,240
JUNIOR ISA	£4,080
HELP TO BUY ISA	£2,400 +£1,000 one-off contribution when the account is opened*

*If you have contributed to a Cash ISA within the 2015-2016 tax year, you won't be able to open a Help to Buy ISA until April 2016 as you can only pay into one Cash ISA per tax year.

WHAT'S IN STORE FOR 2016?

2015 was a bit of a rollercoaster ride for investors. The seemingly relentless rise in house prices and the lack of housing stock, were seldom out of the news headlines. Stock markets around the world experienced jittery periods of volatility in reaction to the economic fortunes of Russia, Greece and China. The 'will they, won't they' saga of potential interest rate rises rumbled on, and UK inflation took an unaccustomed dip into negative territory.

So where do we go from here? In commentary issued last October, Stephanie Flanders, the former BBC economics editor, now Chief Market Strategist for Europe at JP Morgan, urged investors to 'trust in the strength of the economic recovery in the UK.'

She went on to add 'we are now seeing wage growth and we are also seeing productivity growth, which means that each worker is producing more, and interest rates will go up, this is likely to mean that soon it will be a good time for the economy, but a less good time for investors, who might have to get used to lower returns.'

Commentators generally predict that UK interest rates are unlikely to rise in the near term, but that there might be a 0.25% rise over the next twelve months. Inflation is forecast to remain low for the foreseeable future.

What seems clear is that the omens for the UK economy are presently good. For 2016, the International Monetary Fund (IMF) predicts UK growth at 2.2%. It expects to see continued steady growth supported by lower oil prices and continued recovery in wage growth.

WHAT INVESTORS NEED TO CONSIDER

The basic principles of sound investment remain constant. It pays to have a diversified portfolio with a mix of equities, bonds, property and cash, with a good market spread. We will, it seems, have to get used to more market volatility and be realistic about likely investment returns.

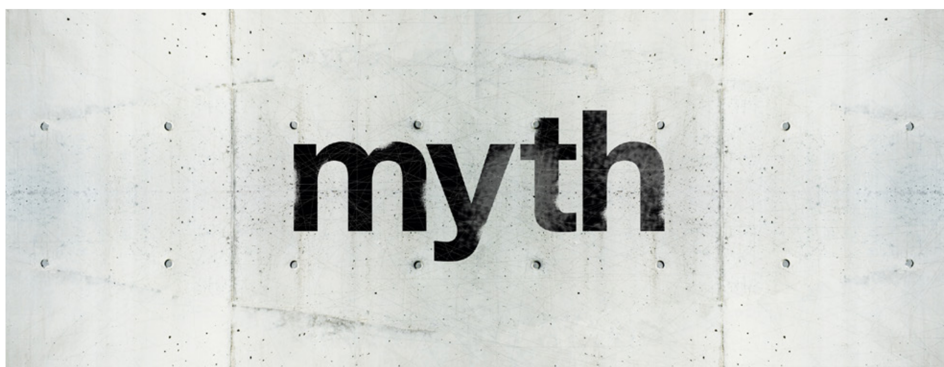
As ever, the mantra that it's 'time in the market' rather than 'timing the market' rings true. Viewing investment as a medium to long-term strategy will help to iron out the inevitable peaks and troughs that markets experience.

If your investment goals or your attitude to risk have changed and it's been a while since you last reviewed your portfolio, why not arrange one now?

The value of investments and income from them may go down. You may not get back the original amount invested.

PENSION MYTHS DISPELLED

Following the wide range of changes in pension legislation, we could all be forgiven for feeling a little shell-shocked as a result. Here we consider some of the myths and misconceptions that have built up around pensions, and help you differentiate fact from fiction.



MYTH: I'VE SAVED A BIT AND THE STATE WILL SUPPORT ME

Although the government has announced an increase in the basic state pension, with an ageing population and other calls on its finances, it is unlikely that the state pension will ever be more than a supplementary buffer and cannot be solely relied upon to ensure a comfortable retirement. Even if you have saved into your own pension, you might not have saved enough to provide the level of income you might be looking for in retirement. Average earnings in the UK are around £26,500, and to match this figure you are likely to need a pension pot of around £400,000. It is well worth talking to your adviser to clarify if your pension planning remains on track.

MYTH: ANNUITIES ARE DEFUNCT

Under the new pension rules, no-one has to buy an annuity. However, for some people, being able to guarantee a fixed income during their lifetime, and that of their spouse, could offer the financial security they require. Don't write off annuities just yet.

MYTH: I CAN RETIRE AT 50 AND TAKE MY WHOLE PENSION POT IN CASH

No. Firstly the new pension changes apply only to defined contribution (DC) pension plans and not to employer schemes. If you have a DC pension plan, the retirement age is 55, not 50. And whilst you could in theory take the entire pot as cash, this could mean you end up paying tax at the top rate. Only 25% of the fund can be taken as a tax-free lump sum, if you withdraw more than this, the income you take will be added to your other income for that year, when calculating the rate of tax you will pay.

A pension is a long-term investment. The fund value may fluctuate and can go down. Your eventual income may depend on the size of the fund at retirement, future interest rates and tax legislation.

INHERITING AN ISA ALLOWANCE

New rules mean that Individual Savings Accounts (ISAs) and their tax benefits can be passed on to civil partners or spouses on death.

Prior to the changes being introduced, any savings held in an ISA automatically lost their tax-free status when the account holder died. This meant that the surviving partner was liable to tax on any income or returns they earned from these accounts. As many people had saved for a considerable number of years, carefully using each year's tax-free allowance to build up their savings, this could amount to a considerable sum. This situation was viewed by many as unjust because ISAs had been promoted on the basis of their generous tax benefits, but lost this status on death.

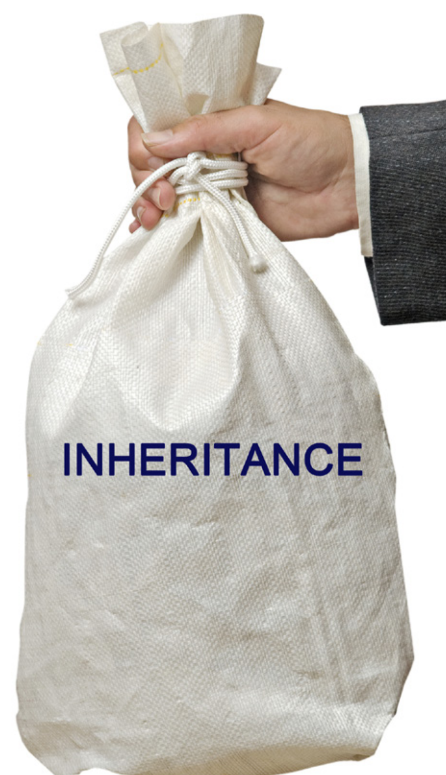
When the government announced these changes, it did so to ensure that bereaved individuals could continue to enjoy the tax advantages they had previously shared with their partner, offering them more flexibility and a much fairer outcome.

THE RULES THAT APPLY

Now when an ISA holder dies, the surviving spouse or civil partner receives an additional allowance called an 'additional permitted subscription' (APS), limited to the value of the deceased's ISA at the date of death This is a one-off allowance which is added to the survivor's own ISA limit.

For example, if the deceased had an ISA worth £70,000 on their death, the surviving spouse will be able to make an APS to their own ISA of up to £70,000, in addition to their own ISA allowance for the year. Even if the ISA is left according to the deceased's Will to someone else to inherit, a son or daughter maybe, the surviving spouse is still entitled to an APS of £70,000, in this instance, although they would need to use their own money to fund it.

Anyone whose spouse or civil partner died after 3 December 2014 is eligible. The APS allowance can be added to a Cash ISA and/or Stocks and Shares ISA, and this can be with the original ISA provider or an alternative provider who accepts APS subscriptions.



KEEPING ON TOP OF THE NUMBERS

During 2015, there were umpteen surveys conducted that suggested that many of us weren't particularly clued up when it came to knowing the important personal financial data that affects our lives. Ask the man or woman in the street what they're paying monthly for their mobile phone and they might manage the correct answer; however, ask what rate of interest they're being charged on their mortgage or credit card debt, and the answer might not be so readily forthcoming. Here are some numbers it pays to be on top of.

YOUR NET WORTH

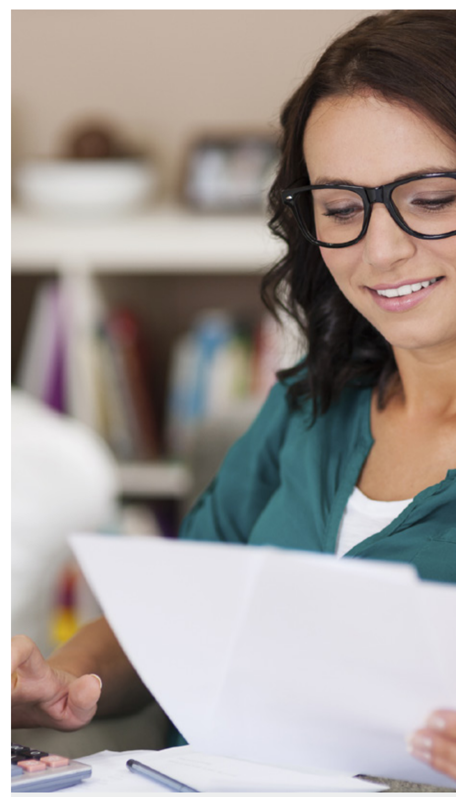
This figure is simply the value of everything you own minus the value of everything you owe. This simple calculation is a good benchmark and will help you track from year to year how your finances are doing. It will show if you're making progress in building and creating financial security. It can help those nearing retirement to plan their future finances, consider their Inheritance tax position, and ensure they don't give too much money away to children and grandchildren at the expense of their own comfort in retirement.

YOUR SAVINGS RATE

This is the amount you save as a percentage of your gross income. Again, it's a way of benchmarking your progress and will tell you at a glance what sort of buffer you have built up to protect yourself against an unexpected drop in income or an increase in interest rates. As you might expect, there are a number of opinions when it comes to the percentage you should aim to put away – anywhere from 10% to 30%. By doing some budget analysis you will be able to see how much you can realistically afford to save.

THE INTEREST RATE YOU'RE PAYING ON YOUR MORTGAGE AND WHEN YOUR CURRENT DEAL ENDS

Although interest rates are currently low, they are predicted to rise in the next year or so.



Knowing these facts will help you plan ahead and get the best mortgage deal for your needs.

WHAT IS AN ETF?

You may have heard the term, but wondered what it meant in practice. Exchange-Traded Funds (ETFs) are investment funds that are listed on an exchange and bought and sold like equities.

ETFs are best described as somewhere between Investment Trusts and Unit Trusts and have been widely available for many years. Like Unit Trusts and Open Ended Investment Companies they are open-ended, meaning you can buy or sell them at any point, and their price directly reflects the underlying investments they hold.

They can be held inside a portfolio, Individual Savings Account (ISA) or a Self-Invested Personal Pension (SIPP).

It's important to note that some ETFs are non UK domiciled and so aren't covered by the Financial Services Compensation Scheme.

HOW DO THEY WORK?

By investing in an ETF, the investor can gain exposure to a range of equities, fixed income stocks, currencies, or commodities without the need to invest in a large number of individual holdings. This means that the investor only pays for a single transaction instead of paying for multiple purchases.

Many ETFs are index funds that replicate an equity or bond index and offer exposure to indices such as the FTSE 100, S&P 500 or fixed income indices, gold, or even specific sectors such as global energy stocks or emerging markets.

Their aim is to provide investors with the same return as the market they are shadowing. For example, if the FTSE 100 goes up by 7% in a year, an ETF that tracked this index should provide investors with the same return, minus fees.

BENEFITS FOR INVESTORS

ETFs offer investors a simple way of diversifying risk in a cost-efficient manner. Spreading risk is a key principle in any investor's portfolio and helps reduce the danger of being vulnerable to a fall in the price of an individual stock or bond. They also reduce their exposure to the volatility that an individual shareholding might experience.

The value of investments and income from them may go down. You may not get back the original amount invested. Some funds will carry greater risks in return for higher potential rewards. Investment in emerging market funds can involve greater risks than is customarily associated with funds that invest in developed, more established markets. Above average price movements can be expected and the value of these funds may change suddenly.

RETRO BUT STILL RELEVANT – POUND-COST AVERAGING

This concept was first developed in the USA, where dollar-cost averaging has been a cornerstone of investment strategy for many years. When markets are going through periods of volatility, pound-cost averaging (PCA) is often advocated as a way to help smooth out the peaks and troughs.

It's all about buying shares of a stock or fund in equal pound amounts at regular intervals. Many investors and finance professionals have long advocated this approach. The advantage is that by investing a given amount over a period of time and in equal-sized amounts rather than all at once, the investor could end up buying more shares when prices are cheaper and fewer when prices are higher. This averages out the buying price of the investment.

Here's an example. If you invested £9,000 in a lump sum and bought shares valued at £10, you'd have a holding of 900 shares. If instead you invested £500 a month for 18 months, you would buy 50 shares in the first month. If the shares went down to £9.50 in month two, your money would buy 52 shares. This means that rather than your whole lump sum of £9,000 being affected by the drop in share price, only a small proportion drops in value. After 18 months, the share price may have returned to £10. By investing regularly you could end up with more shares, despite the share price ending up at the same level as when you initially started investing.

Of course, there are downsides as well as upsides in adopting this strategy.

PLUS POINTS

- When markets are volatile, pound-cost averaging can reduce your risk and potential losses
- This approach means that you don't have to worry about getting the timing of purchases exactly right. There's no need to constantly watch markets to invest at the right moment.
- PCA can give a better outcome than investing a lump sum at the wrong time and watching the value of your investment drop
- By spreading out contributions at regular intervals, you are limiting your exposure by keeping some of your funds in cash

MINUSES

- There is less chance to profit from investing when markets are at their lowest point
- There is ultimately no guarantee that the return will be greater than a one-off investment

Investors need a certain amount of self-control not to cancel or suspend their regular investments when markets continue to fall. You also need to consider that it may cost more to make regular rather than one-off investments.

Remember that all investments carry risk and that prices can go down as well as up, meaning that you could lose money whether you invest regularly or in one lump sum.

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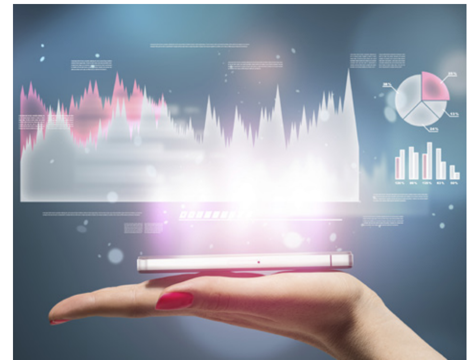

CYCLICAL v DEFENSIVE STOCKS – THE TERMINOLOGY EXPLAINED

Investors have no control over the economic cycle but they have control over the selection of investments in their portfolio. Understanding how different industries react to economic fluctuations is important from a stock selection perspective, as some sectors are more vulnerable than others to fluctuations.

Defensive industries include utilities, household and personal care. These companies produce or distribute goods and services we need, such as food, water and gas; and as a result are defended against the effects of economic downturn. These non-cyclical companies are not correlated to the economy and tend to remain stable during various phases of the economic cycle. In a recessionary environment, they often perform better than the market but during an economic upturn they often perform below the market.

Cyclical companies produce things we can live without and include industries such as manufacturing, travel and automobile. If the economy is strong, cyclical stocks thrive because people have disposable income to spend on luxuries. During a recession, cyclical companies are affected and profits tend to drop along with the share price. Cyclical companies are highly correlated to economic conditions.

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