



360

from **AW Financial Management**



March 2023

Welcome to our Spring edition of 360. We are delighted to share with you the additions to our team here at AWFM on page 4 of this newsletter. It has been a privilege to welcome many of our clients to our new offices at The Old Exchange since we moved in about 9 months ago.

With Easter almost upon us, we particularly remember with gratitude the life and death of our Lord Jesus Christ, who came to bring salvation to all. We pray you will have a blessed Easter.

A very difficult 2022

The term “annus horribilis” was popularised by Her Majesty Queen Elizabeth in 1992, mainly as a result of multiple problems within her family.

It feels apt therefore that in 2022, some 30 years later, that the term could well be applied to investment markets and to personal finance, all of which to some extent pale into insignificance when measured up to the personal suffering for those in Ukraine especially.

But focussing on personal finance, inflation went above 10%, interest rates rose faster and quicker than previously thought, wage demands spiralled as workers understandably struggled to pay their home energy bills, on top of the increase in their mortgage monthly payments, on top of the general cost of groceries.

Meanwhile following the disastrous mini-budget in October, Gilt values which were already coming under pressure, fell still further. The UK Gilt sector, the traditional home for low risk funds, fell by an average of 25% over the course of the year!

Equity valuations in the US fell dramatically where in dollar terms the S&P 500 fell 18% whilst the higher risk Technology related index fell nearly 33%.

At the time of writing, it is hoped that the collapse of Silicon Valley Bank, followed by the takeover of struggling Credit Suisse will not spread into a full-blown banking crisis, given the significantly increased financial strength of the major banks since 2008. 2023 had been looking quite positive until this news broke early in March. Please read the article on page 2 for more details.

We continue to be reassured by the fact that Governments in the UK, US and now Switzerland have intervened swiftly to seek to ensure that nobody who has placed savings in these banking organisations have lost money (though some institutional investors have). Nonetheless, as we write, it does feel as though we may be in for a rough ride over the coming months, as this all works through the system.

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Global Markets and Your Portfolio

This table reflects performance of the ten AWFM-managed investment strategies over the course of the last 3 and 12 months.

The 3 month numbers reveal a positive return across the board regardless of the risk profile. Importantly the returns are scaled broadly according to the risk profiles. The higher risk portfolios have typically produced better returns than the lower risk models.

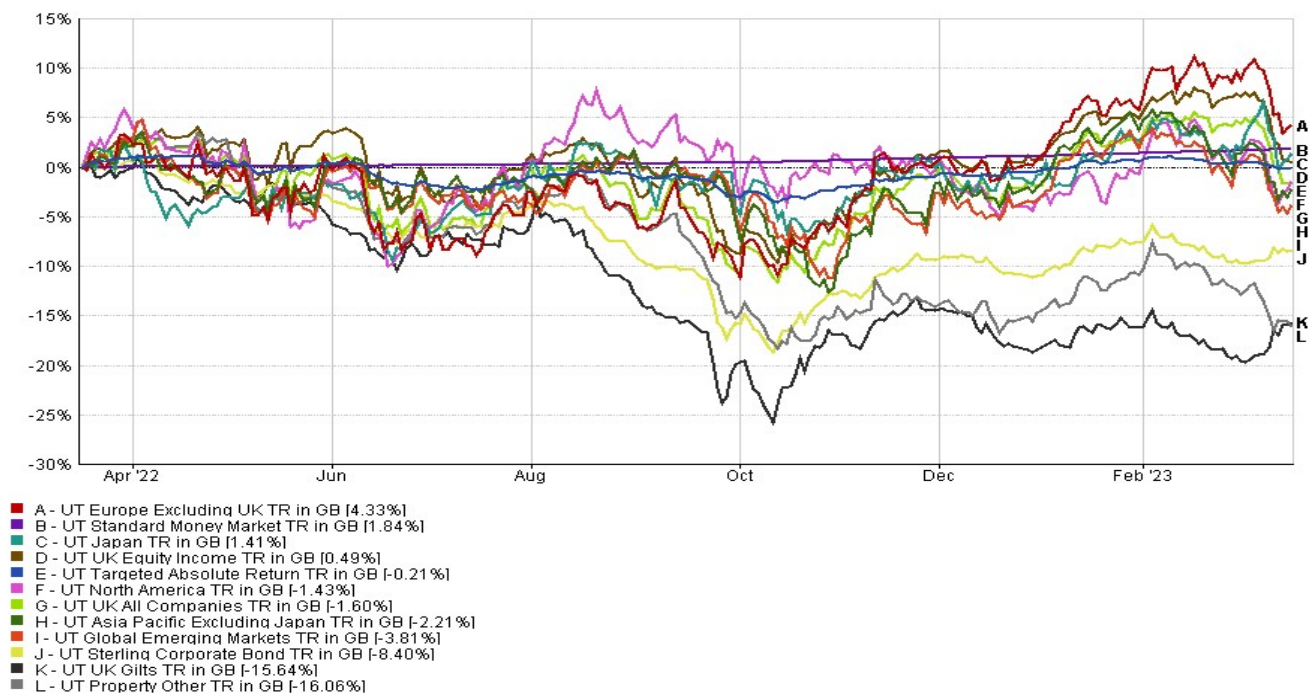
The 12 month figures show the reverse was true throughout most of 2022, where the lower risk portfolios actually lost more than their higher risk counterparts. This is of course unusual and is a factor of the fall in the value of Gilts and Corporate Bonds, both of which were hit (even more than Equity valuations) from rapidly rising interest rates.

Although ethical funds have struggled in 2022, as tobacco, oil and armament stocks were some of the best performers, the difference in returns between Ethical portfolios and those with no ethical overlay has been relatively subtle (when compared to divergence in returns between investment sectors—e.g. Oil vs. Technology).

Description	AWFM Risk Model	Ethical		Unrestricted	
		3m	1yr	3m	1yr
Low Risk	1	1.63%	-7.06%	1.53%	-7.22%
Low to Medium Risk	2	2.29%	-4.83%	2.13%	-5.58%
Medium Risk	3	2.46%	-3.82%	2.39%	-4.40%
Medium to High Risk	4	2.06%	-3.19%	3.01%	-2.26%
High Risk	5	3.43%	-2.04%	4.00%	-4.26%

“But God demonstrates his own love for us in this; while we were still sinners, Christ died for us” - Romans Chapter 5 verse 8.

Investment Returns & Outlook



17/03/2022 - 17/03/2023 Data from FE fundinfo 2023

Fund Manager Consensus Views		
POS	A POSITIVE outlook	UK equity, Pacific Basin (ex Japan) equity, Emerging Markets equity and UK Corporate Bonds.
NEU	A NEUTRAL outlook	UK Smaller Cos equity, US Smaller Cos equity, Japanese Equity, Emerging Markets equity, Property, UK Government bonds ('gilts') and UK Corporate Bonds.
NEG	A NEGATIVE outlook	US equity and European Equity.

Unsurprisingly, Property funds were particularly hit by the rapidly rising interest rate environment we found ourselves in last year, as people grappled with the significant increased cost of mortgages. The sharp increase in interest rates also hit the Fixed Interest markets hard (such as the Sterling Corporate Bond sector shown above), with the lowest yielding Gilts falling the furthest, despite arguably being the lowest risk investment. When a 10 year loan to the UK Government (a 10 year-Gilt) was yielding just 0.50% per annum back in early 2022, and interest rates were at 0.50%, all things were broadly equal. However, with the Bank of England interest rate rising to 4.25%, Gilts started to look increasingly less attractive. Now Gilt value have fallen, a 10 year Gilt now yields 3.35% which broadly reflects what most investors can obtain in bank savings accounts.

Positive returns emanated from just a couple of sectors, most notably and perhaps surprising was the European Equity sector, after a strong 6 months. Back in February 2022 European stocks were heavily sold off following the Russian invasion of Ukraine, both due to the proximity to the war but also due to Europe's heavy reliance on Russia for Oil. However, now that the war enters its second year, with little sign of change, and after investors have assessed the share prices as cheap, and the forecast potential recession in Europe looking less severe than first thought, investors have been moving back into European stocks, driving their prices higher.

What's Happening With The Banks!?

The collapse of the Silicon Valley (SVB), Signature and Silvergate banks (all US) in February this year very much spooked the markets. SVB had been the 16th largest bank in the US and specialised in lending to tech companies. It had an unusually high level of uninsured deposits and lots of investments in long-term government bonds and mortgage-backed securities, whose values had tumbled as interest rates rose.

After SVB reported its fourth-quarter earnings results in early 2023, credit rating agency Moody's warned that it risked getting its credit rating downgraded, in part because it had huge unrealised losses (assets that had decreased in price but hadn't yet been sold) sitting on its balance sheet. This spooked its customers who started withdrawing their money in droves. When they tried to take out a quarter of SVB's total deposits in a single day, it couldn't meet these requests and the bank was shut down. The response from US policymakers was swift: all SVB's depositors (even those with deposits above the \$250,000 federal deposit insurance limit) will get their money back. In the UK, the Bank of England, with the Chancellor's assistance it seems, were able to organise the takeover of the UK branch of SVB by HSBC for £1, securing UK banking customer's deposits.



Nevertheless, the collapse of SVB and its smaller peers (Silvergate Bank and Signature Bank –each of which had a lot of exposure to highly volatile cryptocurrency) sparked general jitters about the health of the banking sector. After several days of wild swings in the prices of lots of bank stocks and bonds and huge leaps in the prices of many banks' credit-default swaps (instruments that allow investors to protect their bond holdings against default), the much larger Swiss banking giant Credit Suisse was in the eye of the storm.....(continued on page 4).

The Spring Statement—Impact on Pensions especially

Another year, another Chancellor and another Budget Statement although this one was more interesting (well, at least for Financial Advisers!) than the majority we have commented on in recent years. Prior to Jeremy Hunt getting to his feet last Wednesday, there had been much trailed speculation that the Pension Lifetime Allowance for pension savings was to be substantially increased - ostensibly as an incentive for 'economically inactive' over-50s to return to the workplace. Quite unexpectedly, however, it's being scrapped altogether from 2024/25 and, in the meantime from 5th April, exceeding the current limit will no longer incur the Lifetime Allowance charge. This was increasingly becoming a problem for many of our clients where benefits over the £1,073,100 threshold would have been taxed at age 75 or when the threshold was breached.

As well as removing the lifetime limit on pension savings, the Annual Allowance for pension contributions is to be increased from £40,000 to £60,000 from 2023/24 – a 50% increase. There was further relief for the very high earners caught by the Tapered Annual Allowance, which reduces the amount they can contribute as a maximum pension contribution. The lower level of the Tapered Annual Allowance will be increased from £4,000 to £10,000 p.a.

Even those who have already *flexibly* accessed their pensions, but wish to make further tax-efficient contributions, benefited as the Money Purchase Annual Allowance increases their maximum annual contribution also from £4,000 to £10,000 p.a.

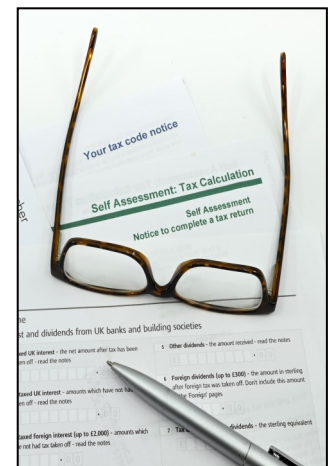
One key issue that was less trumpeted by the Chancellor was the fact that the allowance for withdrawing tax free cash ("Pension Commencement Lump Sum" in today's parlance) has been capped at 25% of the current Pension Lifetime Allowance of £1,073,100. So the maximum tax free cash from a pension fund going forward is going to be £268,275 regardless of the size of pension fund accumulated. This could potentially act as a disincentive to add significantly to Pensions where a fund value is already in or around the current Lifetime Allowance.

One thing that has not changed is the level of complexity around planning for retirement, the risk of poor and irreversible decisions and the need for qualified independent advice.

In other Budget news, there was reconfirmation of changes announced in the Autumn Statement due to take effect from 6th April and all of the important allowances and rates are set out below with changes from the 2022/23 tax year highlighted.

Tax Tables

Income Tax		
Main personal allowances and reliefs	23/24	22/23
Personal allowance* (set to be frozen until 2028)	£12,570	£12,570
Marriage/civil partner's transferable allowance	£1,260	£1,260
Married couple's/civil partner's allowance at 10% ¹ :		
(if at least one born before 6/4/35) – maximum	£10,375	£9,415
- minimum	£4,010	£3,640
Blind person's allowance	£2,870	£2,600
Rent-a-room relief	£7,500	£7,500
Property allowance and trading allowance (each)	£1,000	£1,000
*Personal allowance reduced by £1 for every £2 of adjusted net income over £100,000. ¹ Married couple's/civil partner's allowance reduced by £1 for every £2 of adjusted net income over £31,400 until minimum reached.		



UK taxpayers (excluding Scottish taxpayers') non-dividend, non-savings income	23/24	22/23
20% basic rate on first slice of taxable income up to	£37,700	£37,700
40% higher rate on next slice of taxable income over	£37,700	£37,700
45% additional rate on taxable income over	£125,140	£150,000
Dividend and savings income		
Starting rate at 0% on band of savings income up to**	£5,000	£5,000
Personal savings allowance at 0%: Basic rate	£1,000	£1,000
Higher rate	£500	£500
Additional rate	£0	£0
Dividend allowance at 0% (to reduce again in 2024—to £500)	£1,000	£2,000
Tax rates on dividend income:		
Basic rate	8.75%	7.5%
Higher rate	33.75%	32.5%
Additional rate	39.35%	38.1%
Capital Gains		
Annual Exempt Amount (to reduce again in 2024—to £3,000)	£6,000	£12,300
Main Rate (Basic / Higher Rates)	10%/20%	10%/20%
Residential Property	18%/28%	18%/28%

What's Happening With The Banks?

Credit Suisse is deemed systemically important to the global banking system. Among Europe's biggest banks, it arguably stands out for attracting relentlessly negative headlines about its financial stability over the last couple of years. It's been plagued by series of big losses and scandals, including huge losses and regulatory fines linked to its funding of collapsed supply chain finance firm Greensill Capital and hedge fund Archegos Capital. It announced a radical overhaul of its business late last year that was intended to turn its fortunes around. But its customers – mainly very wealthy people and businesses – had been pulling money out of the bank for months, leading to more than £100bn in outflows late last year. Its announcement in mid-March that it had identified "material weaknesses" in its financial reporting might, at any other time, have seemed just another misstep. But this coincided with peak investor jitters about banking's next weakest link. Investors scrambled to sell its shares, plunging its share price to an all-time low. Switzerland's central bank and regulators responded by forcing Credit Suisse's larger rival UBS to take it over.



Is this another financial crisis? When interest rates and bond yields rise rapidly – and this has been the fastest US tightening cycle since the early 1980s – strains nearly always show up somewhere in the financial system. Although its precise circumstances were very different, the crisis in UK pension funds' LDI (liability-driven investment) strategies last autumn (remember Truss-enomics?!) was, like SVB's woes, driven by the forced selling of longer-dated government bonds as bond yields rose very rapidly. The prices of government bonds with many years till maturity are particularly sensitive to changes in prevailing interest rates. Holding these long-dated bonds which are worth less today than when you bought them isn't a problem if you can hold on to them until they mature: it becomes a problem if you're forced to sell them and crystallise unrealised losses.

As we've explained, policymakers have stepped in quickly to try ease the strains on the banking sector. The Fed has announced a new facility to help US banks: they can now swap assets for cash with the Fed at face value, i.e. what they would get at maturity, not what the market price of the asset is today. And Switzerland's central bank has supported Credit Suisse emphatically. The largest banks globally are much better capitalised now than they were ahead of the Global Financial Crisis (GFC), giving them much greater capacity to absorb losses. In addition, our investment managers don't see evidence of widespread risky lending to borrowers with poor credit quality, or broader credit 'bubbles', as was the case before the GFC. There hasn't, for example, been a comparable surge in consumer borrowing.

In short, we think that a GFC-like systemic financial crisis that might put bank depositors at risk is very unlikely. First, the response from policymakers has been fast and decisive. Secondly, the strongest US, European and UK banks don't share the specific weaknesses of SVB, Signature, Silvergate or Credit Suisse. This isn't a situation where lots of banks have been engaging in similar risky lending practices. And, finally, we don't currently see the key hallmarks that have preceded systemic banking crises in the past. However, lenders around the world are likely to turn more cautious. Banks began tightening their lending standards significantly late last year, and that trend is likely to continue, making it tougher for households and businesses to borrow. This raises the (already high) risk of a global recession. More signs of stress are likely to pop up elsewhere before the current interest rate hiking cycle is through, particularly in areas where interest rate sensitivity is concentrated.

It's likely to remain a bumpy ride!



Laura and Lisa are taking on part-time roles (3 days a week) and looking to assist with our general administration. Caleb and Harry are looking to start new careers with a view to becoming Paraplanners (supporting the partners of the firm in technical matters) in due course. This now takes us to a position where we have a good level of cover at all times in the office, and we are well placed to provide you with a good service in good time.

We are aiming to continue slowly and organically growing the firm over the coming years, with our new office providing us an excellent base from which to do so. If you have not yet visited the new office in pretty Farningham (the picture above was taken from Farningham Woods looking down to the village), and happen to be passing, do feel free to pop in for a tea or coffee and a quick tour. We will be delighted to see you.

New Beginnings

As reported in our December newsletter, we had three of our staff leave in the second half of 2022 to further their careers. Since then we have been on the recruitment drive and are pleased that after Caleb joined us in January, Laura only last week, we will also have Harry and Lisa starting from April and May respectively. I'm sure you will all look forward to meeting our new joiners in due course.

Contact us

w: www.awfm.co.uk
t: 01322 669059

Partners:

martin@awfm.co.uk
jon@awfm.co.uk
sean@awfm.co.uk

Support Staff:

harin@awfm.co.uk
nicola@awfm.co.uk
kiki@awfm.co.uk
caleb@awfm.co.uk
laura@awfm.co.uk

**The Old Exchange,
3 London Road,
Farningham,
Kent,
DA4 0JP**

If you have any questions about this newsletter or your existing investments, please contact us to discuss your situation further.

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