# 360

from **AW Financial Management**

**April 2017**


## In this issue



*Happy Easter!* Welcome to our April 2017 edition of 360. This is our quarterly update on all things financial and we hope you find the articles, reports and commentary both useful and informative.

## The Two Certainties in Life

Perhaps not the sunniest note on which to open our Easter bulletin but, nevertheless, the planned changes to probate fees have caused, in some quarters, an outcry and accusations of a new 'death tax' in disguise. Anyone who has had the responsibility of administering an estate will be aware that, generally speaking, the assets of the deceased are frozen until a Grant of Probate has been obtained from the Probate Registry. Hitherto, this has incurred a flat fee of £155 where a solicitor has been instructed to apply or £215 for personal applications.

However, in February the government announced that as from May (date still to be finalised) the fee — note this is definitely not a tax — will be linked to the value of the estate. The table below illustrates that, although for the very smallest estates there will be no fee, for the most wealthy, the change amounts to an increase of 9,000 per cent.

| Value of Estate before IHT | Proposed fee |
|---|---|
| Up to £50k or exempt | £0 |
| Exceeds £50k but less than £300k | £300 |
| Exceeds £300k but less than £500k | £1,000 |
| Exceeds £500k but less than £1m | £4,000 |
| Exceeds £1m but less than £1.6m | £8,000 |
| Exceeds £1.6m but less than £2m | £12,000 |
| Above £2m | £20,000 |

The Ministry of Justice (MoJ) estimates that, in total, this measure is expected to raise an additional £300m revenue which they say will be used for investment in the justice system. Critics have also described it as a stealth tax and, despite the MoJ's prior consultation which evidenced a majority opposed the proposals, the government seems unlikely to acquiesce as it did over the very short lived National Insurance Contribution reforms announced in the budget. For some illiquid estates there will be concerns about funding this fee and, although the inheritance tax may be paid in instalments (subject to interest on the outstanding balance) it is unclear how some Executors will fund the increased fee as it will not be subject to a similar concession. Benjamin Franklin's oft quoted observation about the only two certainties in life remains apt!

## Global markets and your portfolio

As reported in our October edition of 360, positive returns have again been generated across all of our model portfolios over both three and twelve months. Total returns (capital growth and income reinvested) for the periods ending 24th March are shown here and indeed, in each category they are an improvement on those we saw then. As then, the table shows, more adventurous investors have been more greatly rewarded for taking on more risk during this continued bull run.

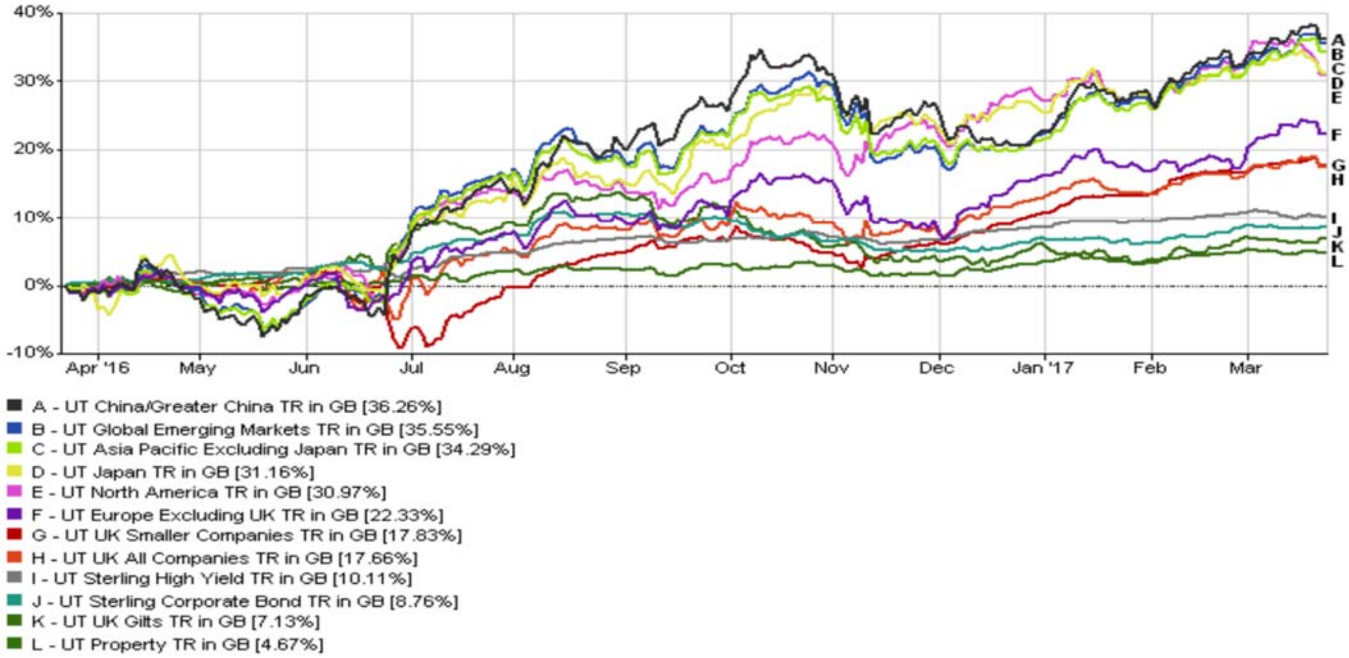
| Description | AWFM Risk Model | Ethical 3m | Ethical 1yr | Unrestricted 3m | Unrestricted 1yr |
|---|---|---|---|---|---|
| Cautious Risk | 1 | 1.93% | 6.35% | 2.03% | 8.26% |
| Cautious to Moderate Risk | 2 | 3.52% | 11.88% | 3.56% | 13.82% |
| Moderate Risk | 3 | 3.94% | 12.86% | 3.78% | 16.82% |
| Moderate to Adventurous Risk | 4 | 4.46% | 17.45% | 4.87% | 21.42% |
| Adventurous Risk | 5 | 5.49% | 23.49% | 5.99% | 26.34% |

In our July 2016 issue, we also explained the differential in returns between our ethical and unrestricted portfolios and, although as you see, the latter have again outperformed, we are pleased to see that the margin has narrowed - largely as a result of the resurgence in sentiment for mid-sized UK business benefiting from the weaker pound and consequent export growth.

*"For what I received I passed onto you as of first importance: that Christ died for our sins according to the Scriptures, that he was buried, that he was raised on the third day according to the Scriptures and that he appeared to Peter and then to the Twelve." - 1 Corinthians 15:3-6*

# Investment returns & outlook

In previous newsletters, we have commented on the currency contribution to investment performance since Brexit and the subsequent decline in sterling which over the last year remains down by just over 13%. The chart below shows returns for the various sectors over the last year although as we write (24th March) during the last three months of this period, we have seen the pound regain some ground and appreciate by just under 2% against the US dollar. This is despite the 0.25% hike in US interest rates in March which would usually be supportive of the latter currency but which was expected and taken as a sign of confidence in the US economy. However, at the same time the pound lost around 1.5% against the euro but nevertheless the FTSE, which measures the value of Britain's top 100 companies by market capitalisation, has over the same period appreciated by just under 5%. This accounts for a general mood of cautious optimism on this side of the Atlantic and that not all of the return is currency gain —again reflected by the overall 32% return in North America.




Even though here in the UK the long heralded triggering of Article 50 of the Lisbon Treaty is set to happen on 29 March and there remains a shroud of uncertainty over what will occur in the next 700 days of negotiations , the resilience of UK markets has been reflected in the performance of our managed portfolios depicted on page 1 of this bulletin which are all biased towards UK exposure.

However, there may be storm clouds gathering on the other side as we write and optimism around the so called 'Trump Trade' dissipates. Markets seem to be digesting Congress's rejection of the President's campaign pledge to abolish Obamacare. It is too early to know if this will have lasting effects for US equities but we remain comfortable with our exposure—ranging between 10-35% in our portfolios—to the world's largest economy as part of our well diversified approach.

Returning to Europe, where we have around 7-17% of exposure in our portfolios, there also remains the prospect of political uncertainty with elections due in Germany and France that could further undermine the EU alliance. Angela Merkel's initial stance towards the UK's impending separation was conciliatory and perhaps mindful of the German automotive industry's reliance on its UK market. However, in recent weeks this stance has hardened somewhat perhaps reflecting concerns that a tide of emboldened anti-EU sentiment may prevail amongst these electorates and threaten to unravel the whole European project. Against this, however, the recent election in the Netherlands saw the PVV fail to live up to initial expectations and this is seen by some as positive news for the European economy.

| | | |
|---|---|---|
| POS | **A POSITIVE outlook** | European Equity & Japan |
| NEU | **A NEUTRAL outlook** | UK Smaller Companies; US Equity; US Smaller Companies; Pacific Basin (excl Japan); Emerging Markets; Global Property & UK Corporate Bonds |
| NEG | **A NEGATIVE outlook** | UK Equity; UK Gilts (Government Bonds) & Global Bonds |

As you see in this table, European equity is currently one of only two asset classes regarded with a consensus of positive sentiment in a poll of fund managers by Old Mutual Wealth. Both Europe and Japan were viewed positively when we last reported but property has moved to a neutral outlook and UK equity and Global bonds are the other areas which show a change of mood as they have declined from a neutral to negative view. We will of course continue to monitor events and any alterations in our stance for AWFM-managed portfolios will of course be notified to you at our next asset allocation review and similarly, for Discretionary Managed Portfolios, your portfolio manager will be keeping you and us abreast as they adjust portfolios when necessary.

As ever, there are many factors at play and, with the latest CPI inflation reading at 2.4% it is becoming impossible to maintain the real value of your capital without taking on a degree of risk—as you will have to varying extents in any portfolio. However, as we have said many times before diversification and the ability to take a long term view should help mitigate that risk whilst offering scope to outpace inflation over the long term.

## The Pound in Your Pocket


Time to start looking down the backs of your settee for any of those 433 million £1 coins which the Treasury estimate are lurking there and under furniture! From Tuesday 28 March, the new dodecagonal shaped replacement comes in to circulation and from **15th October (be warned)** the old version will no longer be legal tender.

This is also bad news for the counterfeiters as the revised design includes sophisticated security measures such as micro lettering around the rim and another feature which has not been disclosed. According to the Royal Mint, there are currently around 45 million fake £1 coins currently in circulation but this new version they say will be the most secure coin in the world.

Let's hope that retailers are able to complete the massive task of adjusting millions of vending machines between now and the October deadline!

## Making Tax Digital

Not only was there good news for the self-employed as the government (somewhat farcically) rowed back from its decision to increase Class 4 NICs announced in the Budget but in the statement there was also respite in the timetable to digitise the tax system.

The plan for businesses to keep digital tax records and to submit quarterly returns by computer or smartphone was scheduled to be implemented from April 2018. However, in response to concerns voiced about timescales, the Chancellor announced that implementation will now be deferred until April 2019 for those with annual turnover of less than the £83,000 VAT registration threshold. Those with turnover of less than £10,000 are exempted from the changes.

Although delayed, the government remains clear in its intention to move to a digitised system for businesses and individuals to register, submit returns and pay tax through a secure online tax account. Although it is estimated by HMRC that the total cost of transition will amount to £430m for UK businesses, they are confident that in the long term the changes will be cost-saving although this is challenged by Federation of Small Businesses. Under the current plans, this means that by 2020 most businesses, self-employed individuals and landlords will be required to use software or apps to keep digital business records and to make regular updates regarding their income tax, VAT and NICs online.

## No Change to Pensions Tax Relief — For Now.

It may seem like Groundhog Day as we again highlight the possibility of further tinkering with the tax reliefs on pension contributions. Whilst the further restriction to the Money Purchase Annual Allowance (see page 4) is set to be implemented, there were no changes either to the standard Annual or Lifetime Allowances for pension savings.

As the government re-emphasised its quest to challenge all forms of tax avoidance, pension planning remains one of the few legitimate opportunities for tax-efficient investment. We have noticed a significant increase in enquiries which stem from the much publicised pensions freedom whilst at the same time the government grapples with the problem of an ageing population coupled with insufficient retirement provision. However, some commentators also note that the decision to scrap planned NIC increases leaves a £2bn hole in the nation's finances whilst the estimated net annual cost of pensions tax relief amounts to £25bn. Whilst the Treasury consulted on this question last year and saw no need for changes, much of the relief is received by the highest earners—and as the changes to Probate Registry fees indicate (see page 1) - there may be appetite to limit the reliefs received by them to help plug the hole.

As ever, good advice in what is still a very complex area of planning will be worth its weight in gold and we have a number of tools at our disposal devised to help our clients achieve their goals in a tax efficient manner.

## Spring 2017 Budget

On 8th March, Philip Hammond presented his first— and last — Spring Budget. As flagged last year in his first Autumn statement, future budget statements will be delivered in the Autumn. Some measures announced last year were re-confirmed but here are the highlights:

- A short-lived proposal to increase NICs for the self-employed—a move which was subject to a U-Turn a week later
- Reduction in the annual tax free dividend allowance from £5,000 to £2,000 as of 6th April 2018
- The rate for the new NS&I Investment Bond announced as 2.2% per annum fixed for 3 years and accommodating investment of up to £3,000 available from April 2017
- Reduction of the Money Purchase Annual Allowance which restricts pension contributions for those who have flexibly accessed pension benefits from £10,000 to £4,000 per annum
- Personal Allowance up from £11,000 to £11,500 and basic rate Band from £32,000 to £33,500
- The transferable Tax Allowance ('Marriage Allowance') which enables a basic rate tax-paying spouse to receive unused personal allowance from the other to increase from £1,100 to £1,150
- As explained in detail in our April 2016 edition the Lifetime ISA ('LISA') - which enables £4,000 per annum to be saved and supplemented with a 25% contribution from the Government - is set to be available from 6th April 2017 although at the time of writing many providers are holding off on new products until the rules are finalised

As ever, tax continues to be at the heart of much financial planning and whilst there is no substitute for professional tax advice we continue to incorporate complex tax calculations in to our planning discussions with clients.

## The Residence Nil Rate Band (RNRB)

Another previously announced measure which takes effect from the 2017/18 tax year is the introduction of the Residence Nil Rate Band. Introduced to alleviate the increasing burden of inheritance tax (IHT) on homeowners as properties are more often breaching the £325,000 nil rate band for IHT, this will provide an additional allowance to escape IHT. Although the property on which the allowance is claimed does not have to be the main family home, it has to have been a residence of the deceased at some time. The new allowance will increase over the next four tax years as shown on the left.

| Tax Year | RNRB |
|---|---|
| 2017/18 | £100,000 |
| 2018/19 | £125,000 |
| 2019/20 | £150,000 |
| 2020/21 | £175,000 |

In order to qualify for the allowance, the property must pass to a direct descendant but for estates valued at more than £2m, the RNRB will be tapered away at the rate of £1 for every £2 by which this threshold is exceeded. However, for many married couples the new allowance means a combined nil rate band of £850,000 in 2017/18 rising to £1m in 2010/21.

As we find in our conversations with clients, IHT and estate planning are very personal issues and opinions vary dramatically from one to the next. However, it is fair to say that not everyone is aware of the extent to which IHT can bite and this is something which we can help to quantify if and when it becomes part of your planning priorities.

## AWFM News

Of course the big news from our perspective (apart from Martin's milestone birthday!) is that we moved office and are now reasonably well settled in our new offices (over) and overlooking the River Cray. There are always teething difficulties with any such move but mercifully they have been few in number.

At the time of writing we are still waiting for the main contractor to undertake some final snagging to the office space but we have all adapted to our new surroundings well. Martin now has a 10 minute drive to work which he is managing, Jon has a similar commute as before, but Sean (who found us the office) is now able to walk to work through the Spring-laden streets of Sidcup!

In development terms, Edward has now managed to pass the first of six exams leading him to qualification, as has David. Sean has also taken the opportunity to brush up on his Pension knowledge passing the relevant exam.



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