RT FINANCIAL PLANNERS LTD

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Volatility in Investment Markets

I had considered writing about Brexit and the effect different outcomes may have on markets, but trying to anticipate the outcome, let alone give any meaningful insight, is almost impossible and likely to be outdated by the time this newsletter reaches you! So I felt it better to simply address market volatility, which has undoubtedly been heightened in recent times and I believe that this may well continue for some time yet.

It is undeniably true and also quite understandable that short-term losses can prick an investor's emotions, as no-one likes to see their portfolio go down in value, but staying in the market and resisting the temptation to cash-out is more likely to pay off in the end. Of course, in certain circumstances, there may be very valid reasons for considering encashing, or a reduction in risk, but there are also many reasons why it may very often be better to sit tight and take no action.

There are two points I wish to make – one is that long-term investing helps alleviate short-term falls in value and the other is that it is impossible to time markets - and that trying to do so can lead to heavy losses.

So I would like to stress that the longer the term over which investments are held, the more significant will be the increased chance of positive returns. As a firm we have looked in some detail at the considerable data supporting the argument for long-term investing.

Looking at global stock market data between January 1970 and July 2017, if you had randomly picked one day during this period and chosen to invest just for that one day, you would have had a 53.5% chance of making gains — almost a similar odd to the toss of a coin. But long-term investing dramatically increases your chances of making positive returns. If you had invested your money for one month during that same period, your chances of making a profit increased to 62.8%. Investing for any one year during that period would have generated a positive return 77.8% of the time, while investing for ten years increased your chances to 98.6%. Interestingly, an investor who invested in the stock market for more than 11.1 years at any point in time during this period never lost money.[1]

It is clear that any falls in value in the first year of an investment can be stressful, because a year in isolation is more likely to show losses than a longer timeframe.

These early days are when anyone new to investing may feel stressed about the ups and downs in financial markets. But the likelihood of making a loss should go down over time and with it so can the feelings of anxiety as one becomes more familiar with the natural ebb and flow of market prices. It is worth remembering that what might seem like a big sudden movement on day one can appear as a small blip when viewed over the course of several years.

We must also remember that it is a fact that, from time to time, stock markets will go through periods of uncertainty and although the sharp falls which can be experienced at these times are understandably unsettling for investors, this is quite usual at times. Those who sell or delay making new investments when stock markets become uncertain are employing a strategy known as 'market timing'.

The intention of this strategy is often to invest once stock markets have calmed down, or to buy when stock markets have gone even lower. However, this can be a very dangerous strategy, partly because sharp falls in stock markets tend to be concentrated over short periods of time. Similarly, the biggest gains are often clustered together. It is also quite common for a large gain to follow a big fall (or vice versa). So, an investor who tries to anticipate when is the best time to invest, runs a high risk of missing the best gains, which can have a big impact on their long-term return.

To illustrate this, Fidelity analysed the average annual return from the UK stock market over the last 15 years and it showed that missing just the ten best days over this period would have cut an investor's annual return substantially. From the end of June 2003 to June 2018, they found that had one remained fully invested in the FTSE All-Share, the return would have been 8.9% per year. This is reduced to 4.6% by missing out on the best 10 days and to just 2.0% by missing the best 20 days. These are annualised figures so very substantial differences.[2]

Of course, none of us know without the benefit of hindsight when the best or worst days will be – which underlines why timing the stock market is so difficult (if not impossible) and reinforces the point that the best policy is usually to stay fully invested over the long term.

Please do bear in mind that past performance is not a guarantee of future performance – and as with all investments the value of your money can go down as well as up.

Sources

[1] Macrobond; MSCI World Equity Mid and Large Cap Total Return in GBP, 1 January 1970-31 July 2017
[2] Fidelity Investment Services;

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Helping Grandchildren onto the Property Ladder

Rising property prices and sky-high university fees means that today's young adults are finding it increasingly difficult to buy their first home, and we are seeing more grandparents coming to the rescue. Many grandparents leave money in their wills for their grandchildren, but by making that gift during their lifetime, they can personally see the benefit it has on their family.

Making a gift at the earliest possible time means that investment growth can play a bigger part in meeting the ever-increasing costs and - from the grandparents' perspective - the gift will be outside their estate for Inheritance Tax (IHT) sooner. There may however be an understandable concern about giving grandchildren too much too soon, so careful thought needs to be given to the best way to pass on wealth and hold and invest it until it's needed.

For many years, 'designated accounts' have been a way of earmarking money in Investment Funds for a grandchild without them actually receiving it. Funds can then be transferred to the grandchild at the appropriate time, but for tax purposes the designation must be deemed irrevocable, which can prove inflexible.

Making a gift into trust may ease the fears of giving large sums to grandchildren before they have sufficient financial maturity and can provide grandparents with the control they seek. This will mean understanding what type of trust to use.

Absolute or Bare trusts are the simplest form of trust. But they are also the most restrictive. The beneficiaries cannot be amended if circumstances change and they are legally entitled to the money once they reach 18. But there are tax advantages of using Absolute trusts. The initial gift is a potentially exempt transfer with no immediate IHT. Income and gains will be assessed upon the beneficiary, meaning they'll be able to use their own allowances and tax rates. In addition, the gift will be outside the grandparent's estate for IHT after seven years.

Discretionary trusts are often preferred as they provide greater control over when and how the money is distributed and they're typically flexible enough to allow any future grandchildren to benefit. In contrast to the Absolute trust, the initial gift is a chargeable transfer, but there will be no immediate IHT charge payable, provided the grandparents have enough nil-rate band available. This means a joint gift of up to £650,000 can be made without a charge. However, control within trusts does come at a price, and Discretionary trusts pay higher tax rates. Onshore or Offshore Investment Bonds in the trust can simplify matters for trustees of a Discretionary trust as they have no income or gains to account for during the investment term and when the money is needed policy segments can be assigned to the grandchild, once they're over 18, who will then become the person taxed on subsequent surrender.

So the right combination of trust and investment wrapper can ease grandparents' concerns about gifting large sums to their grandchildren at a young and impressionable age. An Investment Bond held in a Discretionary trust can combine the necessary control with a tax-efficient investment solution.

A Reminder about Sharing Income Tax Allowances

According to HMRC three million UK couples have already taken advantage of the Marriage Allowance, but a million more are still eligible for the free tax break.

If this figure is accurate it means that more than a million married and civil-partnered couples are still eligible for the free tax break, which is worth up to £238 this year. And thanks to the start of the new tax year couples can backdate their allowance and boost their payment up to £900 – just in time for Christmas shopping!

To recap, the Marriage Allowance is available for married couples or those in a civil partnership and where one partner doesn't earn anything, or their income is £11,850 or less (or they are for other reasons a non-taxpayer), and the other partner's income is between £11,851 and £46,350 (or £43,430 if in Scotland).

It won't affect the application for Marriage Allowance if the applicant or their partner is currently receiving a pension, or live abroad - as long as they receive a Personal Allowance.

Applying for the Marriage Allowance is quick and easy and once an application is complete it is processed immediately. The new online form takes less than ten minutes to fill out and eligible customers will receive backdated claims of up to £662 as a lump sum. Couples have four years to claim their backdated allowance.

It should be noted that if the applicant or their partner was born before 6 April 193, they might benefit more as a couple by applying for Married Couple's Allowance instead. It is not possible to get Marriage Allowance and Married Couple's Allowance at the same time.

A Brief Reminder About Pension Death Benefits

I have addressed this matter on a number of occasions, but it is important and as such I make no apologies for the degree of repetition.

Pension funds may now play a greater role in transferring wealth between generations, since the changes in how death benefits are taxed and who can benefit. This means it is more important than ever that your wishes on what you want to happen to any remaining pension funds on death are correctly recorded, to ensure everything is in place to have your money put in the right hands with the least amount of tax payable. Please ensure your adviser knows your wishes, and please advise us if these change so we can update your instructions as appropriate.