PARTNERS WEALTH MANAGEMENT

PWM Insights

Planning your financial freedom (September 2021)

Welcome to the latest edition of PWM Insights.

In this edition, we will look at the subject of cash vs inflation, and why more people are turning to investments.

In addition, we take a look some of the potential issues arising from the change in pension age which comes into force in 2028.

Finally, we also reflect on a couple of issues that have come across the desk over the last few months that might add quick value.

Beating inflation – is cash still king?

As the economy re-opens following the various lockdowns of the last 18 months, we expect more attention in the upcoming months to be focussed on the topic of potential inflation pressures in the UK and overseas.

This has led us to consider inflation and its impact, and how to ensure that the real value (or purchasing power) of your capital is not eroded by it.

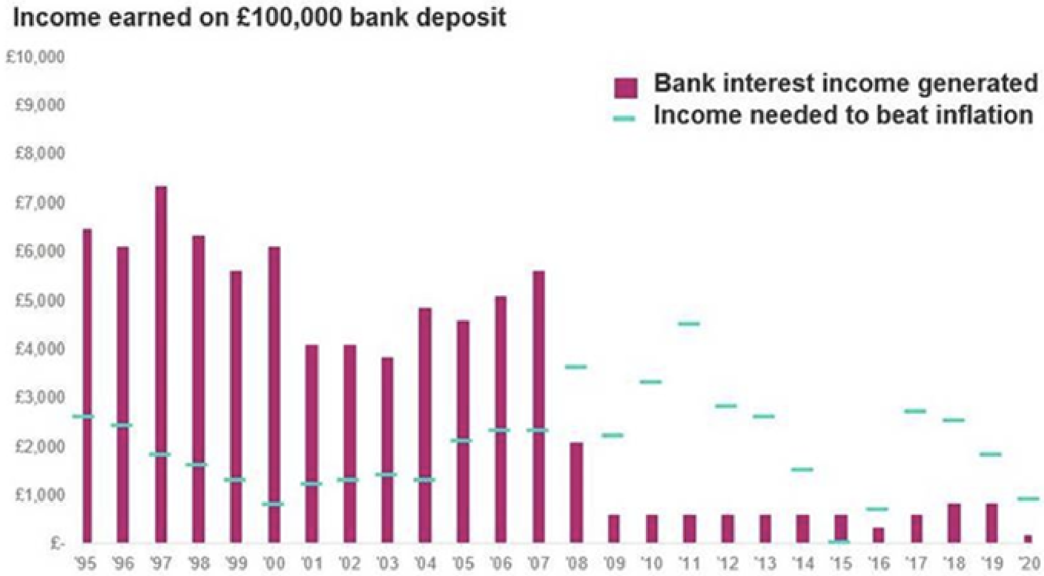
Isn't inflation low historically?

The short answer to this is yes. Over the last 20 years (to the end of 2020), inflation averaged 2.8% per annum, whereas in the previous 20 years (1980-2000) it averaged 4.8% per annum.

However, even at this low level, inflation is not to be overlooked.While we might not feel the impact of something costing £102.80 that last year cost £100, the cumulative effect of inflation over the low inflation period of the last 20 years to 2020 means that goods and services which would have cost £100 in 2000, would cost £172.13 today (from 1980 to 2000, the increase would have been from £100 to £254.76). (*Source for all inflation data: Bank of England)*

Does the return on my cash savings keep pace with inflation?

The chart below compares savings rates each year (on £100,000), and the level of return required from savings to beat inflation. Interestingly, from 2008 the rate of return from cash accounts is significantly lower than the inflation beating level, which means that cash investors over the last 13 years have seen the real value of their capital fall year after year.



Source: 7IM, Bloomberg Finance L.P.

So, if the returns from deposits are not good, should I hold cash?
We advise all our clients to hold some of their wealth as cash, with the level dependent on individual circumstances, attitudes to risk and their perceived expenditure over the coming period.

As a general rule, we advise our clients to hold around 1-2 years' perceived expenditure as cash, so investments do not need to be sold to meet living expenses in the event of investment market volatility. While this might expose these deposits to losing their "real" value, this is an invaluable step and has provided our clients with a huge amount of reassurance historically during investment market falls (such as in early 2020 during the start of the COVID-19 pandemic).

It could be debated that keeping in excess of two years of expenditure as cash could expose too much wealth to an unnecessary loss in purchasing power due to inflation, if you are holding significantly higher levels of cash you may wish to consider deploying this in a way that will keep pace or beat inflation over the longer term.

In conclusion
Although everyone's thoughts about deposits and investments will be different, the impact of inflation should not be underestimated. If you would like to learn more, please get in touch to explore this topic in greater detail and we can help build a plan of action to make your money work harder for you.

Pension age change – is this something that requires action?

From 2028 the minimum state pension age will increase from 65 to 67, and alongside this, the minimum age at which you can draw from your own pension arrangements will increase from 55 to 57. This is likely to impact on those born after 6 April 1973 (or those aged 48 and under).

Over the recent weeks, the Government has confirmed that in certain circumstances it will still be possible to take benefits from the age of 55, which are summarised as follows:

- Members of "uniformed pension schemes" (including armed forces, police and fire services) will retain a normal minimum pension age of 55;
- The right to take benefits at an earlier age is retained on a 'block transfer' (whereby two or more people transmit from the same transferring scheme to the same destination scheme at the same time).
- An individual member of a registered pension scheme who (on 5 April 2023) has a right to take benefits from an earlier age than 57, and the rules of the scheme on 11 February 2021 (which was the date of the original consultation into the increase in pension age) gave a right to take benefits at an earlier age, can retain the right to take benefits at age 55.

Focusing on the last point, there is an expectation that those affected by this change could start trying to source a pension that will allow them to retire earlier, or that there could be a call to action from some in the advice sector to try to move clients' pensions into such a scheme. However, the question that should perhaps be considered first is "do you need the flexibility to draw from your pension before 57?"

We all appreciate the idea of enhanced flexibility will be attractive, and the thought of having someone tell us to "wait a bit longer" to draw on something that might have seemed a lifetime away when we started saving is less so. However, it would be sensible to remember the following points before rushing ahead:

- Pensions are a fantastic intergenerational inheritance tax planning vehicle. Since pension flexibilities were announced in 2016, it has been possible to pass a pension fund to next and future generations without there being an assessment for inheritance tax. If assets need to be drawn upon, would it make more sense to use an asset that would be subject to inheritance tax in the future, rather than draw from your pension?
- Do you envisage that at any point before the age of 57 where you can stop (or will want to stop) working, and need the ability to draw on your pension?

- Depending on how you access benefits from your pension, you could severely limit the amount you can save to pensions in the future if your intention is to "catch-up" again in the future.
- If you believe you may want to draw on your pension, how do you envisage using the funds? Perhaps it may be better catered for elsewhere to retain the tax efficient benefits provided by the pension?
- Having a retirement age of 55 "baked into the policy rules" would be something that was arbitrary at the point rules were written. Such schemes might have less flexible and inferior investment options or higher charges, and there might be advice and set-up fees associated with a move to such a scheme.

In conclusion
While the option to retain the ability to draw pension earlier than 57 is advantageous, the question for many should be whether their circumstances require drawing pension benefits at such an early stage.

If you would like to discuss the upcoming changes in the context of your individual circumstances and consider whether action of any kind is required, please get in touch.

Food for thought

Selling your rental property/second home – tax is due 30 days after

If you are selling a property which is not your principle private residence, capital gains tax (CGT) is due 30 days after the sale completes.

This is a very tight deadline, and it is imperative that you speak to your accountant early in the process, as this needs to be registered separately via a "Capital Gains on UK Property Account" (i.e. not via your normal self-assessment). Registering this account can be time consuming, and liaising with your accountant early in the process will help avoid potential penalties and interest that will accumulate after the 30-day deadline.

Separation and CGT implications

The timing of a separation can have an impact on the financial planning aspects of the separation. If the transfer of assets between spouses and civil partners who have been living together takes place in the same tax year to the separation, the transfer will not be considered at market value, and, therefore, does not attract CGT; whereas there will be a CGT assessment if assets are transferred in a different tax year.

Therefore, a couple permanently separating on the first day of the tax year (6 April) will have a whole year in which plan and transfer assets without CGT, whereas a couple doing the same toward the end of the tax year will have very little time to make the best decisions.

If you would like to discuss this further we will help support you through this difficult time and, where appropriate, work alongside one of our trusted contacts within the family law sector.

I hope that this update is useful and informative, if you have any questions regarding any part of this, please contact me or your Partners Wealth Management adviser.

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