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FINANCIAL SERVICES

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NEWSLETTER

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An overview of auto-enrolment

New research by Scottish Widows shows that over half of eligible employees are unaware of auto-enrolment. Furthermore, while 52 percent of those surveyed – equivalent to almost 10 million employees – were not aware of the reforms, businesses are also struggling with the changes.

According to research conducted on behalf of NEST, the default government scheme, 55 percent of employers with more than 1,000 employees expected to receive a lot of assistance with auto-enrolment, increasing to 58 percent amongst those with between 100 and 999 employees.

Accordingly, with auto-enrolment starting on 1st October 2012, we will now provide a recap of employers' duties under the new regime.

Every employer will be required to automatically enrol all employees aged between 22 and state pension age who earn more than £8,105 into a qualifying workplace pension scheme and make minimum contributions.

These requirements will be phased between October 2012 and February 2018, with a firm's compliance date dependent on the number of people they employ.

Businesses will also be required to provide at least one percent of the two percent minimum contribution level during the introductory phase. This will rise to eight percent by October 2018, with at least three percent contributed by the employer.

Employers will also be required to enrol anyone aged at least 16 but under 75 if the employee requests this. Should these employees earn more than £5,564 per year, businesses will also need to make contributions for them.

However, these qualifying limits are set to be reviewed annually, with the government having already released proposed figures for 2013-14. The earnings trigger is set to rise from £8,105 to £9,205 from 6th April 2013, while employers would need to make contributions for those earning over £5,720.

While planning for auto-enrolment already impacts on businesses in terms of ensuring they have a qualifying pension scheme in place and the costs of complying with this legislation, these changes to the limits will increase the burden on firms with staging dates in the first four months of next year.

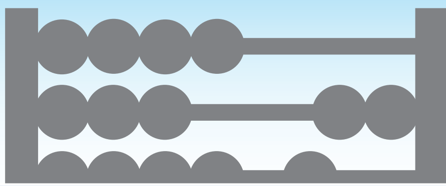
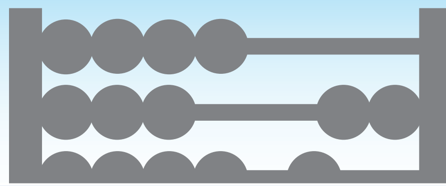
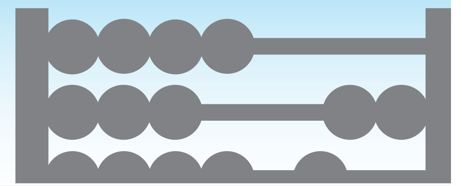
Finally, employees will be able to opt out of auto-enrolment, although it is unlikely that many will choose to do so. Only 11 percent of those who said they were aware of auto-enrolment in the Scottish Widows research planned to opt out.

It would seem, therefore, that those who know about auto-enrolment are following the celebrity entrepreneurs in the government's latest awareness campaign by saying "I'm in".

As you can see, there are many issues to take into account when preparing for auto-enrolment. At Rickard Keen Financial Services, we have the expertise to provide impartial advice on any current pension scheme your company offers, and whether it complies with the forthcoming legislation.

Alternatively, if you are yet to introduce a pension scheme, we can help you set one up and minimise the resultant financial impact on your business.

Therefore, for further information and guidance, please contact us.

Savings and investments: where can you put your money?

The ongoing effects of the global economic crisis continue to make saving and investment decisions challenging. There are lots of different places where investors can put their money, and yet many people are not aware of the full range of options available to them.

The current economic climate has been described by some commentators as one of the worst in history. On top of the recent global financial crisis, the events across North Africa and the Middle East have led to more instability. Furthermore, the eurozone debt crisis is causing severe strains in bank funding and broader financial markets. Add to this the problems of persistently high inflation and the outlook for savers and investors continues to be challenging.

What are the options?

Our round-up looks at the main characteristics of many of the options available to savers and investors in the current climate, and also looks at the potential pitfalls.

First of all, however, it is important to remember that there are differences between saving and investing. Although there are different definitions in use, in simple terms, many of them share the idea that savings products are 'low risk' (you usually get back at least what you put in, and usually interest on top), while investments may offer greater growth but this isn't guaranteed – they could fall in value or you could lose your money altogether.

Savings accounts: Can you beat the effects of tax and inflation?

Bank savings accounts' relative simplicity is attractive to many savers, as is the fact that the value of personal savings up to £85,000 (per regulated firm) held in most bank accounts is protected in the UK by the Financial Services Compensation Scheme (FSCS). However, there are also some pitfalls to savings accounts. For example, in the long term, it may be impossible to 'beat' the combined effects of tax and inflation. In addition, while it may be possible to get a better interest rate by locking your money away for a specified period of time, there is a chance that you could lose out if interest rates increase suddenly.

RKFS says: However, in the present and foreseeable future, interest rates are likely to continue to be low and therefore there is the real prospect of your capital losing value due to inflation.

Individual Savings Accounts (ISAs): Tax-free savings

ISAs offer you a tax-friendly alternative. Every adult can put up to £5,640 a year into a cash ISA, and up to £11,280 into a stocks and shares ISA. Your overall limit is £11,280 per year. There is no tax on the amount of interest you earn but you can only contribute to one cash ISA and one stocks and shares ISA each tax year (the current allowance ends on 5th April 2013). The ISA allowance is set to increase each year with inflation.

What about stock market investments?

The variety of markets and funds (e.g. an investment vehicle that may invest in different types of assets) available to investors has increased over the last twenty years. There is a huge choice of funds available to investors, from funds investing in the shares of companies in specific regions of the world, to funds that focus mainly on generating an income for the investor by identifying companies that pay high dividends (a proportion of company profits paid out to shareholders). Other funds focus more on trying to grow the value of the investments over the longer-term. In practice, not all investments will be suitable for all individuals, so it is important to consider the different options available to you.

More generally, it is believed that company shares (equities) could be a viable option for investors, with the potential to generate good returns over the long term, while acknowledging the risk that long-term growth is not guaranteed, and that you could lose your money if the companies or funds in which you invest do not perform well.

RKFS says: Historically, long-term returns from equities have beaten inflation and those of the other major asset classes (cash, fixed interest and commercial property).

Multi-asset funds: Spreading your money between different types of investment

Given the sharp movements in numerous markets around the world, some investors are avoiding funds that invest in only one asset type, instead choosing funds that can move money between different asset types in response to market conditions. These funds seek to generate steady, total returns (i.e. a return comprised of long-term capital growth and income) with fewer fluctuations than those funds that only invest in one asset type (but which may not offer quite the same potential for growth).

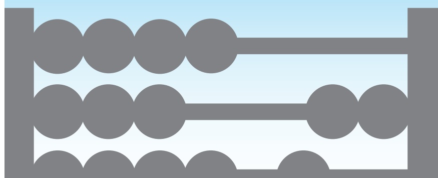
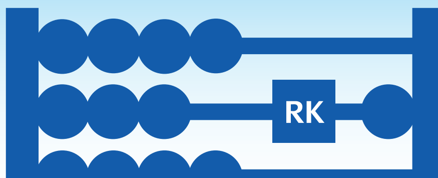
Emerging (stock) markets

Many experts believe that the long-term prospects for emerging economies and their stock markets are more attractive than those for developed nations and markets. Emerging economies typically have much younger populations than their developed peers, giving them large workforces that are able to operate very competitively in the global marketplace.

In contrast, many developed countries are facing the reality of an ever-shrinking workforce that must support the needs of an ever-growing number of retired people. Moreover, as emerging economies develop, their middle classes are likely to continue to grow; this in turn creates a fast-growing base of consumers to buy the products and services of companies based in emerging markets. Furthermore, some emerging economies are blessed with substantial natural resources.

When viewed in combination, it is possible to see how these factors can create a very positive picture of the prospects for emerging countries, and companies based in those countries. Indeed, it is not uncommon for emerging stock markets to see periods of strong growth, as investors react positively to publications of good economic statistics and company financial results. The flipside of this is that emerging stock markets can often fall very quickly if, for example, economic figures are not so good, or when social or political problems rear their heads (as happened recently in the Middle East and North Africa).

For these reasons, those considering a fund that invests in emerging markets will need to remember that the value of their investments can go up and down sharply. It is also important to note that emerging markets have additional risks owing to their less developed market practices.

Government bonds

Almost all governments have requirements to borrow money; one of the ways in which they do this is to issue bonds. Most government bonds are a promise by the government to pay a specified rate of interest to the investor, before returning the original sum borrowed on a specific date in the future.

Bonds can be traded on the financial markets in the same way as other financial assets. If the owner of a bond decides to sell it before the date on which the original sum borrowed is due to be returned, the new purchaser might pay more or less than the 'face' value of the bond – for example, the new owner might pay just 98 pence (or less) for every pound that is ultimately due to be repaid by the government on the specified date in the future. Equally, the new owner might pay 102 pence (or more) for every pound borrowed (the 'face' value).

Either way, the rate of interest payable by the government to the owner of the bond remains the same – it is always a stated proportion of the 'face' value of the bond. The relationship between the fixed interest rate payable on the bond and its price is referred to as the yield; when the price of a bond goes up, the yield will fall, and vice versa.

The price an investor will be willing to pay for a bond will usually reflect numerous considerations, including the prevailing interest rates, as well as an assessment of the ability of the borrower to repay its debts. While government bond prices are often thought of as fluctuating to a lesser degree than some other types of investment such as company shares, no bonds, including government bonds, are immune from the impact of economic influences, and prices can fall as well as rise; this is something which investors in funds that invest in government bonds should bear in mind.

There are also other types of bonds, such as inflation-linked bonds, which have different characteristics, and it is similarly important to remember that investments in bonds issued in foreign currencies entail additional risks, as changing foreign exchange rates can have a material effect on the value of investments.

Corporate bonds

These work in much the same way as government bonds, but instead of lending money to a government the bondholder is lending money to a company. Corporate bond prices are subject to similar influences to government bonds. However, they also carry certain additional risks, the main one being that companies are often considered more likely than governments to 'go bust' and be unable to repay their debts.

The flipside of this is that companies must usually pay investors a higher rate of interest than governments as a way of compensating the investor for the increased risks involved in buying corporate bonds instead of government bonds. Funds specialising in investing in corporate bonds may therefore offer the potential to generate higher returns, but with a potentially greater risk that the investment may fall in value.

Commercial property funds

Commercial property includes a wide range of different types of buildings, such as office blocks, shopping centres and warehouses. Investing in funds that include commercial property can be a useful source of returns, offering the potential to generate both income (through the rents payable by tenants in buildings) and capital growth (if the value of buildings or land rises).

Of course, buildings may remain vacant – meaning no rent is received – and land values can decline as well as rise. In addition, it can be difficult to sell buildings in a rush. One alternative to funds that purchase individual buildings directly is to invest in a property securities fund. These funds invest in the shares of property companies that are traded on the stock market, meaning that the shares can usually be sold with relative ease in the event that the investor requires his or her money back. Naturally, these investments are subject to the same risks as any investment in company shares.

Commodities

Commodities include physical goods and are usually divided into 'hard' and 'soft' commodities. Hard commodities include things like precious metals such as gold and silver, industrial metals like steel and aluminium, and energy sources like oil and coal. Soft commodities include things that are grown, such as coffee, cocoa and meat.

Private investors generally gain access to commodities markets by investing in funds managed by professionals. Commodities may be considered a worthy component of a diversified range of investments, as they can perform in a contrasting way to other investments such as government bonds. However, commodities remain one of the more risky types of investment precisely because they are traded on markets, and therefore prices can fluctuate.

Many commentators have said that savers in their 50s and 60s have been particularly hard hit by the economic downturn. Rising inflation and low interest rates have squeezed spending power and shrunk pension pots. On top of this, annuity rates are at an all-time low. There is no easy way of combating these problems but being well informed is a good start. Therefore, for more information about any of these options, please contact us.

The original version of this article appeared in the January 2012 Money Matters newsletter from BNY Mellon Asset Management. The ISA figures have been updated for the new tax year.

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Summer markets commentary

The global economy has had to deal with a number of knocks in recent months, all of which have had an impact on the ongoing slowdown in economic activity.

The key risks are unchanged – events in Europe, a policy error by the US administration, a hard landing in China and an oil price spike caused by events in the Middle East. Even if all these are avoided, that still leaves us facing a prolonged period of below par growth. Slowing economic activity is likely to lead to disappointment in corporate profits relative to expectations.

According to the latest figures from the Organisation of Economic Co-operation and Development (OECD), the first quarter in 2012 saw growth slow or remain flat in all G20 countries except Australia, Germany, Japan, Korea and Mexico. The report also noted a slowdown in growth in China, India, Indonesia and South Africa.

However, in spite of this, there are many encouraging aspects to the world economy coming from the US in particular, where consumer spending power is well underpinned, the housing market looks to be in recovery and much of the manufacturing is in good shape.

Inflation in both China and Germany fell in June, with the former reaching a 29-month low, according to Chinese government data. Chinese inflation will soon reach its bottom and it is likely that the People's Bank of China will increase the amount of money available for lending, providing further stimulus.

In Germany, consumer prices fell by 0.1 percent in June, bringing inflation down to 1.7 percent. In the past two years, German inflation has been an obstacle to further monetary easing from the European Central Bank, but this problem now appears to be ebbing.

Overall, while the economy slowdown appears entrenched in much of the world, falling inflation seems to be bolstering consumers and may be giving central banks an incentive to ease monetary policy.

Moving in and out of markets is fraught by one factor and that is timing. Rickard Keen Financial Services has always believed in a risk-assessed diversified portfolio invested over the long term. This has, historically, outperformed inflation and higher rate deposit accounts. Past performance though is no guarantee of future returns.

Our view is, to a certain extent, underpinned by a recent article in a book review where Daniel Kahneman, a Nobel Prize winning psychologist, gave an example of an investment firm that asked him to analyse their results. The outcome indicated that when one stock is sold to buy another, the sold stock subsequently outperforms the bought one by 3.2 percent a year. A further study shows that private investors who traded most often had the poorest results.

The portfolios we put together for our clients are reviewed in-house on a quarterly basis, making adjustments as and when appropriate.

Whilst markets remain uncertain our advice is to sit tight or, alternatively, where further capital is available, take advantage of relatively low prices by investing now.

Ensure your fund is not as sick as a dog

As we have already discussed, this year has presented many challenges for investors, making it even more imperative that they chose their funds carefully.

While all funds can have the occasional blip, it is important to identify funds that continue to perform badly, as investing in them over the long term can have a significantly detrimental impact on any portfolio.

However, it does not follow that holdings in these underperforming funds should automatically be sold, as there may be valid reasons why this has happened. Therefore, we would advise you to seek professional advice before taking any action, so please contact us for more information.

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