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Navigating choppy waters

Many people become concerned when they see stock markets displaying the kind of high volatility they have in recent weeks.

Normally, share indices move up or down by less than 1% in a day, but over the course of September, the FTSE 100 Index, which measures the movement of the largest 100 UK-listed companies' share prices, experienced massive turmoil.

Volatility is a response to uncertainty. When there is a broad consensus about the economic outlook, as there was during the economic recovery in 2009, stock markets often develop a steady trend. But when it is not at all clear what is going to happen next, share prices can go through periods of high volatility until a consensus does emerge.

Today, commentators cite two main causes of volatility: the ongoing euro crisis and fears about the pace of global economic growth. In both cases, there are wide differences of opinion about what is likely to happen. Some think a Greek default will lead to the break-up of the euro, others that the eurozone will muddle through. Some think the current slowdown in economic growth in the developed world and China is a temporary interruption of a recovery, others that it signals a recession.

It is important to understand that while stock markets are barometers – they reflect what *is* happening today – they are not that good at predicting what *will* happen. Nobel prizewinning economist Paul Samuelson put it like this: "Commentators quote economic studies alleging that market downturns predicted four out of the last five recessions. That is an understatement. Wall Street indexes predicted nine out of the last five recessions!"

So if you have committed capital to the stock market for the long term as part of a balanced portfolio, you should not be too swayed by day-to-day movements – up or down. Such volatility is the price you pay for returns that have always been, over the long term, higher than those from cash deposits or fixed-interest investments.

And if you are saving regularly, then in fact you may benefit from volatility, since it can lower the average price at which you purchase investments. If you do have concerns about your savings or investments, we will be happy to discuss these with you. Past performance is not a guide to future performance. Investments can go up or down, and you may not get back the original amount invested.

In this issue:

How low can you go?

What risk means to you

Annuity rates continue to shrink

Getting ready for 1 October 2012

Will you live to be 100?

The Junior ISA arrives

Swiss tax agreement to catch evaders

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How low can you go?

The base rate may not have moved, but some other interest rates are hitting ultra-low levels. It may be time to take a closer look at your investments.



The Bank of England base rate has now been 0.5% for over two and a half years and shows no sign of increasing soon. Although short-term rates have attracted most attention, some medium and longer-term interest rates have also been falling. For example, at the start of November 2009 it cost the UK Government 3.67% to borrow money for ten years via gilts (government bonds), whereas the cost two years later had dropped to 2.25%.

Where there have been falls in interest rates, these have had some significant and unwelcome effects.

Income drawdown The rules for income drawdown – drawing an income directly from your pension fund – were revised in April 2011. In many instances, the combination of this change and the decline in long-term gilt yields has substantially reduced the maximum amount that can be drawn per £1,000 of fund. If you have been taking drawdown for some years and are due for a review in the near future, you could find that the maximum you can withdraw will fall by up to 50%, according to a recent press report.

Fixed-term deposit rates Back in October 2008, as the credit crisis peaked, you could have obtained over 7% from a three-year fixed-rate bond. The likelihood that base rates will continue at current levels for some time means that today's fixed-rate offerings are much lower – the best rate for three years is now under 4.50%. National Savings & Investments withdrew their five-year fixed-rate and index-linked savings certificates in early September.

If the decline in yields has affected you, a review of your investments may be worthwhile. The fall in yields has not been universal. For example, over the last year sterling corporate bonds yields have generally increased because of concern about the state of the global economy. The same worries have seen UK share prices fall and dividend yields rise correspondingly since the start of the year.

The value of your investment and the income from it can go down as well as up and you may not get back the full amount you invested. Investing in shares should be regarded as a long-term investment and should fit in with your overall attitude to risk and financial circumstances.

Have you remembered that if you missed the 31 October filing date for your 2010/11 paper tax return, then you must file online by 31 January 2012? The penalties for late filing are now much higher than they used to be – the starting point is £100, even if you owe no tax. 31 January is also the date for paying any outstanding tax due for 2010/11 and the first payment on account for 2011/12. If you expect to pay less income tax for 2011/12 than 2010/11, you can make a claim to reduce your payments on account using HMRC form SA303. The FSA does not regulate tax advice.



What risk means to you

Like most emotive words, 'risk' means different things to different people. When such an emotive word is used in the context of money, it can cause not just anxiety but confusion.

So like most financial advisers today, we try to clarify what 'risk' means – and this is usually as much to do with you as it is to do with what you invest in. Risk is a function not just of prices going up and down, but of your attitudes, needs and circumstances, as well as your capacity for financial loss.

What is a risk profile?

The end product of questionnaires and discussions on the subject of risk is usually called a 'risk profile'. It is the document we, as your advisers, will use as the basis for any savings or investment recommendations we make. Often it will include a short description of the kind of pattern of risk and return you are prepared to accept. Financial advisers generally consider a risk profile should have three components:

Tolerance of risk. This is what you feel about risk and is usually

easy for you to articulate. It is also simple to discover where on the 'risk spectrum' you are by completing a questionnaire and in discussion.

Need for risk. This relates directly to your aims. For example, if you have an ambitious target for early retirement, you may need to generate a high return from your savings in order to have enough capital to generate your target income. In this case you would have to take high levels of risk to achieve what you want.

Capacity for risk. This relates to your circumstances. For example, if you are retired, you cannot replace any capital you lose with income from work, so your capacity for risk is likely to be lower than that of someone who is in employment. We are duty bound to consider especially your capacity for loss.

We will normally create a risk profile based on all three elements to provide clarity about how you plan to meet your goals. A risk profile cannot prevent you from suffering loss, but it may ensure that you understand why you are taking on a certain level of risk, and that if market prices fall, your losses are within a range you can cope with, both practically and emotionally.

Annuity rates continue to shrink

Falling government bond yields and increasing lifespans are pushing down annuity rates.

Annuity rates are currently at the centre of a perfect storm:

- Yields on long-term government bonds are at historically low levels (see 'How low can you go?' on page 2).
- Life expectancy continues to increase rapidly – witness the Government's efforts to increase the state pension age.
- Forthcoming new EU rules are making it more expensive for insurance companies to underwrite annuities.

This means that if you are about to draw benefits from a pension plan, you must review all your retirement income options, including:

Open market annuities You should never accept the annuity rate from your pension plan company without first checking what is on offer elsewhere. Annuity rate setting has become increasingly refined in recent years. For example, some companies now set rates according to your home postcode. If you are a smoker or in less than perfect health, you may be entitled to an enhanced annuity rate.

Phased retirement Phased retirement involves drawing on your pension plan in stages, with each year's 'income' consisting of a tax-free lump sum and annuity payment(s). This route has the advantage of avoiding the one-off annuity purchase, but it does involve more investment risk. Part of your pension plan will remain invested after your retirement income begins and annuity rates could fall further.

Income drawdown Income drawdown – drawing your income directly from your pension fund – is normally only a viable option if you have other sources of retirement income. It can offer considerable flexibility, but in most instances your maximum permitted withdrawal will be much the same as an annuity can provide. Income withdrawal arrangements virtually always carry investment risk and if this concerns you, an annuity could be a better option.

Phased retirement and income drawdown are high risk, complex retirement income strategies. In view of their complexities, it is particularly important that you review your objectives and options with the help of expert pensions advice. The value of your investment and the income from it can go down as well as up and you may not get



back the full amount you invested. The value of tax reliefs depends on your individual circumstances. Tax and pensions laws can change.

Getting ready for 1 October 2012

It may be nearly a year away, but if you are an employer, you should be preparing for 1 October 2012.

Most new laws affecting businesses now start to operate from 6 April or 1 October. Thus 1 October 2011 brought a rise in the national minimum wage, the introduction of new rights for agency workers and the final abolition of the default retirement age.

1 October 2012 will see two more significant changes, which have been long in preparation:

- The start of a four-year phasing in of auto-enrolment – largest firms first – into workplace pension schemes for employees and other workers; and
- The official launch of the National Employment Savings Trust (NEST). NEST has been designed as the default pension where no alternative arrangement is offered by the employer.

Unlike the existing stakeholder pension access arrangements, there will be no exemption for employers with fewer than five employees: if you have just one employee, you could need to auto enrol them in a workplace pension. Broadly speaking, only individuals under age 22, over state pension age or earning less than the personal allowance (£7,475 in 2011/12) are not subject to auto enrolment.

Once an employee is auto-enrolled, you have to make pension contributions unless the employee decides to opt out. (Remember that those who opt-out must be auto-enrolled every three years.)

The minimum employer and total contribution levels are set as a percentage of 'band earnings' and are being phased in over five years (see table below). However, the band has not yet been finalised as the Government is awaiting earnings inflation data. In practice the band is likely to be between about £6,000 and £40,000 a year.

Date	Minimum employer contribution* %	Minimum total contribution* +%
October 2012 – September 2016	1	2
October 2016 – September 2017	2	5
From October 2017	3	8

* Based on band earnings
+ Employer plus employee gross contribution (i.e. including 20% tax relief)

The phasing in of auto-enrolment means that most employers with less than 50 workers will not begin to auto enrol until at least March 2014. That may seem comfortably distant, but many employers will prefer to be ready before the legislation forces them to act.

Will you live to be 100?

The chances of reaching your century are probably greater than you think.

In the summer, the Department for Work and Pensions (DWP) issued some new calculations about the chances of anyone alive today living to the age of 100. Its work briefly grabbed the morning headlines and radio reports on an August day thin on news.

The DWP was probably using a quiet time for the press to garner support for the department's plans for increasing the state pension age. After all, 65 looks like rather an early retirement age if you can hope to live to 100. As the brief extract from the DWP's tables show, in the future the monarchy could be kept very busy with congratulatory messages to centenarians.

Chance of living to 100

Age now	20	30	40	50	60	70
Men	19.5%	16.5%	13.7%	11.4%	9.5%	8.2%
Women	26.6%	23.2%	20%	17%	14.5%	12.6%

Source: DWP August 2011

The fact that at age 60 nearly one in ten men and over one in seven women are expected to reach age 100 is one reason why annuity rates are not as attractive as they once were. Let us know if you want to discuss your financial planning for old age.

The Junior ISA arrives

1 November marked the launch of Junior ISAs.

One of the Government's early spending decisions was to withdraw new Child Trust Funds (CTFs) and replace them with Junior ISAs (JISAs). New CTFs were withdrawn from 3 January 2011 and JISAs came into being on 1 November 2011. JISAs are generally available to any child born before 1 September 2004 or after 2 January 2011. Their main features are:

- Unlike CTFs, there is no government contribution.
- The maximum overall investment is £3,600 per tax year, rising in line with CPI from 2013/14.
- The investment components are the same as adult ISAs – cash or stocks & shares – but there are no restrictions on how a

contribution may be divided between the components so long as the total contributions do not exceed the £3,600 allowance.

- Although the child may manage their own account from the age of 16, no withdrawals are possible before age 18 other than in very limited circumstances.
- The normal ISA tax benefits apply, with no personal liability on income generated from contributions you make as a parent.

The value of your investment and the income from it can go down as well as up and you may not get back the full amount you invested. Investing in shares should be regarded as a long-term investment and should fit in with your overall attitude to risk and financial circumstances. The value of tax reliefs depends on individual circumstances and tax laws can change.

Swiss tax agreement to catch evaders

The UK Treasury has signed an agreement with Switzerland about UK tax evaders.



In these hard-pressed times, HM Treasury is more anxious than ever to collect tax revenue. Its latest effort in this direction has been to reach an agreement (subject to parliamentary approval) with Switzerland concerning funds held in that country by UK taxpayers. The details released so far are that:

- The existing funds of UK taxpayers held in Switzerland will be subject to a one-off deduction of between 19% and 34% to cover past tax liabilities. Those who have already paid the UK taxes due will not be charged.
- A new withholding tax of 48% on investment income and 27% on gains will apply to UK residents with funds in Swiss

bank accounts from 2013. To avoid these charges – which closely correspond with the top rates of tax – the investor would have to authorise a full disclosure of their affairs to HMRC.

- In 2013 a new information sharing provision between the two countries will be introduced. The Treasury believes this will make it easier for HMRC to find out about Swiss accounts held by UK taxpayers.

The Swiss deal is a further reminder that, as well as being illegal, tax evasion does not pay. The FSA does not regulate tax advice and tax laws can change. Levels and bases of, and reliefs from, taxation are subject to change.