CHAMPAIN
FINANCIAL SERVICES

Bawtry
Selsfield Road, Ardingly
Haywards Heath
West Sussex RH17 6TJ

01444 229 520
info@champain.co.uk
www.champain.co.uk

Technical Update No. 88 7th November 2021

All

‘Surprise interest rate pause’

The Bank of England Governor Andrew Bailey is facing a backlash from economists and MPs for 'crying wolf' over an interest rate hike. Critics questioned whether he was the right man to lead the Bank after a 'big communications failure' on interest rates prompted lenders to raise mortgage costs unnecessarily – and sent currency markets into a tailspin. Mr Bailey was also criticised for allowing officials to keep working from home at a time when the economy needs urgent attention due to rising inflation. The Governor had given a strong signal that interest rates were set to rise when he said in October that the Bank 'will have to act' to control inflation, which is now predicted to hit five per cent next year. Yet he surprised economists by recently voting against an increase, and rates were left unchanged at 0.1%. Lenders including HSBC, NatWest and Nationwide had become so convinced by Mr Bailey's earlier comments that they had already pulled their best deals or raised rates in advance of the vote. City investors were also wrong-footed, with the pound sent tumbling against the dollar in its worst week since August. Economist Gerard Lyons, who was previously in the frame for the job as Governor, said millions of borrowers were paying the price for 'poor' communication by the Governor. Commentators have pointed out that It's already led to higher mortgage rates – and so an impact is already being had on people's finances. Mr Bailey, 62, has also come under scrutiny for focusing on issues other than inflation and rates as the country attempts to recover from the pandemic and the price of goods and fuel rises ahead of Christmas.

Property Owner

Mortgage rates creep up despite Bank of England Inaction

Mortgage borrowers' chances of securing an ultra-cheap deal narrowed this week in spite of a decision by the Bank of England to hold interest rates at 0.1%, as banks and building societies raised interest rates across their fixed-rate home loans. The central bank's decision surprised financial markets, which had factored in a rise this month. Rates are nonetheless likely to rise to around 1% by the end of 2022, according to the Bank's inflation report. Lenders, which had already been raising interest rates on their home loans amid expectations the Bank would act, pressed ahead with further withdrawals of low rates. Rate rises on mortgages at HSBC, NatWest and Nationwide took effect on Thursday. Skipton Building Society said it would remove all of its three-year fixed rates on Friday and Leeds Building Society announced a rise in rates on mortgages at loan-to-value ratios of 80 and 85%. For a borrower paying an average standard variable rate on a £150,000 repayment mortgage over 20 years, a rise in rates to 1% would leave them paying an extra £71 a month. The number of sub-1% deals fell from 131 in the first week of October to 30 by November, according to Moneyfacts, the finance website. One lender to withdraw such a rate this week was HSBC, which raised the 0.99% interest rate on its two-year fixed-rate mortgage to 1.14%. Nationwide raised the five-year rate on its 60% LTV deal from 1.24% to 1.34%. Rate rises are set to have less impact on mortgaged households than in the 1990s and 2000s because of long-term growth in fixed-rate mortgages, which protect borrowers from rate rises over the period of the agreed term. Over 90% of mortgages advanced over the past four years have been fixed rate loans.

However, experts believe the impact of a rate rise to 1% in 2022 is unlikely to reverse the recent growth trend in the housing market. Repayments are currently equivalent to 39% of the median full-time salary after tax, below the historical average of 43%. And a rise in interest rates to 1% would only take mortgage repayments up to the long run average.

All

Are we heading for a carbon crash?

So far, the big message from the Glasgow climate conference is the role of finance in decarbonising the global economy. But economic experts have warned that It’s a dangerous development in some respects. In his speech to COP 26, the Chancellor, Rishi Sunak, pledged action to 'rewire the entire financial system for Net Zero.' Finance has taken centre, stage in large part because of inadequate government policies. According to the United Nations Environment Programme, around two-thirds of global emissions are linked to private household activity. Reducing them requires major changes in people’s lifestyles, UNEP says. What’s missing in the march to net zero and ESG (environmental, social and government) investing is beneficiaries. Commentators have cautioned that a financial system wholly geared to financing net zero isn’t one focused on savers and investors. Pension funds exist to generate secure incomes for pensions; insurers need to be solvent to pay out against insurance claims. Neglecting the beneficiary, some say, is a formula for financial ruin. Carney puts the net zero financing requirement at around $100 trillion (£75 trillion). ‘If there’s a revenue stream, then the funding is infinite,' Bank of America chief executive Brian Moynihan told the Wall Street Journal. These revenue streams don’t currently exist, but one way or another, they will be created – supported by governments and multilateral aid agencies such as the World Bank. On the other side of the ledger, returns on investment in the production of hydrocarbon energy needed to keep the lights on and economies moving are to be suppressed, pushing up their cost. The day Sunak spoke, low wind speeds necessitated paying coal-fired power stations thousands of pounds per megawatt hour to help keep the lights on. Historian Adam Tooze calls the energy transition a 'historic experiment.' The climate crisis enters a new, dangerous phase as finance ministers, central bankers, and financial leaders all look to save the planet – with other people’s money.

Investor / Saver / Retired

Millions blocked from accessing pensions at 55

Millions of savers will be blocked from transferring their pensions to access them at age 55 after the Treasury closed a loophole. HM Treasury has clamped down on pension transfers in advance of a planned increase to the minimum age at which savers can access their pension from 55 to 57. From 2028, savers will have to wait an additional two years before they can dip into retirement savings without triggering punitive tax bills. The pensions industry has criticised the plans, warning that some pensions will still be accessible at age 55 while others will be locked until 57. Some schemes explicitly state that savers have an "unqualified right" to take pension benefits at 55 and this will still hold. Originally the Government was to allow savers to free up their pension two years sooner by transferring their retirement pots to a scheme that allowed it. This loophole has since been closed after repeated warnings from experts. One of the problems highlighted by commentators is that millions of savers will now have a mix of pensions, with some pots they can access at age 55, and others where they need to wait to 57 making it harder to plan for retirement. Anyone who made a request to transfer their pension to a pension scheme with a protected pension age of 55 or 56 before Nov 3 will still be able to keep the protection and this change will not affect them. John Glen, the economic secretary to the Treasury, said the Treasury purposefully chose not to announce the change at the Budget last week to avoid a wave of pension transfers ahead of the cut off.”

All

A threat to recovery

Findings of recent surveys show that consumer sentiment has dipped in recent weeks after the outbreak of euphoria when lockdowns were lifted and consumers could once again visit pubs and clothes shops. The Bank of England has noticed too. When Andrew Bailey, the governor, stunned the financial markets by announcing that interest rates would remain at their record low of 0.1%, he pointed to signs of weaker consumer spending as a reason to delay the expected hike to 0.25%. Hopes have been resting on consumers to power the economy out of its deepest contraction in 300 years, as Covid restrictions eased. During those lockdowns, households amassed savings because, with shops and restaurants closed and holidays thwarted by travel restrictions, they could no longer spend in the usual way. According to the Office for Budget Responsibility (OBR), the government's independent fiscal watchdog, those "excess savings" — the total in people's bank accounts above normal — amount to £180 billion, or an average of £6,474 per household. As the harshest of Covid restrictions came to an end this spring, the Bank of England and the Treasury wanted to persuade the public to start eating into their savings. Spend, spend, spend was the rhetoric. It has not yet happened. In fact, deposits with banks and building societies and cash saved in National Savings & Investments accounts rose by £9.4 billion in September, nearly twice the £4.8 billion average increase in the two years before the pandemic. Rob Wood, chief UK economist at Bank of America Merrill Lynch, said it had to be assumed that the public was now saving by choice. And that could be a troubling behavioural trend when it comes to spending longer term. The OBR assumes that households will spend 5% of these extra savings each year for five years; the Bank of England assumes 10% will be spent over three years. Whether consumers spend this money or not is central to whether the Bank needs to hike interest rates. If households keep saving at this rate, the Bank does not need to hike rates. So the motivation of consumers is now facing scrutiny to establish when they might stop building up their savings and spend the cash again, or to gauge whether the habits developed during the lockdowns will persist.

All

How to calculate your 'personal inflation rate'

If you read the headlines, you've probably seen a lot of people fret that inflation is a big problem for the U.K economy right now. But will it actually end up being a big problem for you? The truth is, it all depends on what you spend your money on. The official measure of inflation, based on economists' rough guesses about what most people buy each month, could be very different from the unofficial inflation that you yourself are experiencing. This means if you want to know how much to worry about rising prices, and perhaps whether to budget for them, you need to calculate your own personal rate of inflation beyond what you see talked about in news. It is tempting to think of inflation as a shrinking bank note, as if today's inflation rate meant each pound coin in your wallet would be worth 95 pence the next time you walk into a store. But the so-called headline rate is really just a one size-fits-all average that can disguise the fact that prices for some goods are ballooning dramatically, while prices for others may be static or even falling. Whether inflation ends up taking a bigger or smaller amount from your budget depends on what your expenses are. A good example right now is energy prices, which are among the biggest catalysts for inflation. If you're not driving, you're not directly impacted by higher fuel costs for a car. Of course, a non-driver may still be affected indirectly by higher fuel costs because it could cost more to take public transportation, get an Uber or transport items to stores. But the pain of paying more money to fill up your tank at the petrol station won't be felt equally by drivers and non-drivers alike. To calculate your personal inflation rate, experts recommend analysing how your annual spending can be divided between eight broad categories — food, housing, apparel, transportation, medical care, recreation and leisure, education and communication, and other goods. (It may help if you already use a budgeting app or if your credit card categorizes expenses for you.) With that information, you can then input your spending for each category into a worksheet and update the current inflation rates for each category. This personalised inflation rate will help you to understand how inflation impacts both your spending and your savings. While inflation will eat into any money that you have in a savings account, your investments may not take much of a hit. That's because stocks historically have outperformed the rate of inflation.

Retired

How to legally cut your IHT bill

Inheritance Tax is a tax on the property, money and possessions of someone who's died and, after the Chancellor froze the threshold at which people pay it in his 2021 Spring Budget, concerns were growing that he was getting ready to make further changes to pay for the COVID-19 pandemic. That hasn't happened, yet. Currently, Inheritance Tax must be paid if the entire value of someone's assets exceeds £325,000, with the levy charged only on the part above this cut-off. This threshold increases by an additional £175,000 allowance per person if an individual is leaving their main home to children or grandchildren. There are things people can do now to make sure their loved ones pay less in tax when they pass away:

1) **Make a will** - First and foremost to benefit from the £175,000 allowance that can be used when leaving the main residence to children or grandchildren, Britons need to make a will.

2) **Spend more money** - An easy way to avoid paying IHT is to not get caught out in the first place.

3) **Sell assets or downsize** - Selling the main residence could benefit people

4) **Gifting while alive** - People can give gifts of up to £3,000 per year and carry any unused annual exemption forward for one year. They can also make small gifts to the value of £250 for each child per annum.

5) **Put pensions and protections in trusts** - Pensions can play a big role in estate planning, as they aren't included when IHT is calculated.

6) **Consider leaving money to charity** - in some cases leaving money to charity could reduce someone's IHT.

Investor / Saver / Parent

What to do with your Junior ISA

This week marks the 10 year anniversary of the Junior Isa, which may lead some parents to reflect on whether the tax free savings account has led to some meaningful returns. Three fifths of junior Isas are held in cash, according to research by F&C Investment Trust. However, it appears returns regret has bitten some parents - upon realising the financial returns missed by saving, a third of those parents say they wished they had invested the money instead. Among Interactive Investor account holders, of those who invested in stocks and shares Jisas there are 110 with a value of more than £100,000 and a further 1,078 with between £50,000 and £100,000. Junior Isas can be opened for any child living in the UK under the age of 18 and parents can contribute up to £9,000 each tax year. Parents can either opt to use the tax-free wrapper to either save or invest towards their child's future. With savings in a cash Jisa all interest earned will be shielded from tax, while those who invest in a stocks and shares Jisa will be shielding any dividends or capital gains from the taxman. Almost half of parents favour the cash Jisa because they think it is a safer option than investing, according to F&C Investment Trust. Junior cash Isas also offer parents better returns than other savings vehicles with the benefit of higher interest - all of which is tax free. The average monthly payment into a Jisa is £87 a month, according to Hargreaves Lansdown. If you kept up the payments for ten years, and your investments returned long-term growth of 5% a year, you could build up £13,510. If you kept it up for the full 18 years, you'd have £30,381 by the end. But some investments over the long term can achieve even greater returns than this. According to investing platform Interactive Investor, the top three most held stocks in Jisas over £50,000 are Scottish Mortgage Investment Trust, Fundsmith Equity and F&C Investment Trust. Someone who invested in Scottish Mortgage Investment Trust exactly five years ago would have seen a return of almost 400% ignoring platform charges, management charges and dividend payments. Those who invested in Fundsmith Equity or F&C Investment Trust five years ago would have seen 124% and 80% growth respectively. An investment of £25 a month in F&C Investment Trust over the past 18 years would have grown to £17,646, If the same had been done via the average easy-access savings account, based on Moneyfacts data over the past 18 years, the final return would have been £5,854 - more than three times less. Those trying to weigh up between saving or investing in a Jisa will likely consider the past performance of various funds or investment trusts - albeit understanding that past performance is no guarantee for the future. Financial planners and investing experts often use 5% as the type of annual return you can expect over the long term - to some this may not be tempting enough to take the risk. But an element of investing that perhaps isn't mentioned enough is the power of compounding that investors and even savers can benefit from, especially over the long-term when investing for children.

Past performance is not a guarantee to future performance. You may get back less than invested.

Thresholds, percentage rates and tax legislation may change in subsequent Finance Acts and reliefs from taxation are subject to change. The FCA does not regulate tax advice.

The content of this newsletter is for information only. It does not represent personal advice or a personal recommendation and should not be interpreted as such. Please do not act upon any part of it without first having consulted an Independent Financial Adviser.

For information about our services please contact Champain or view online.

END