

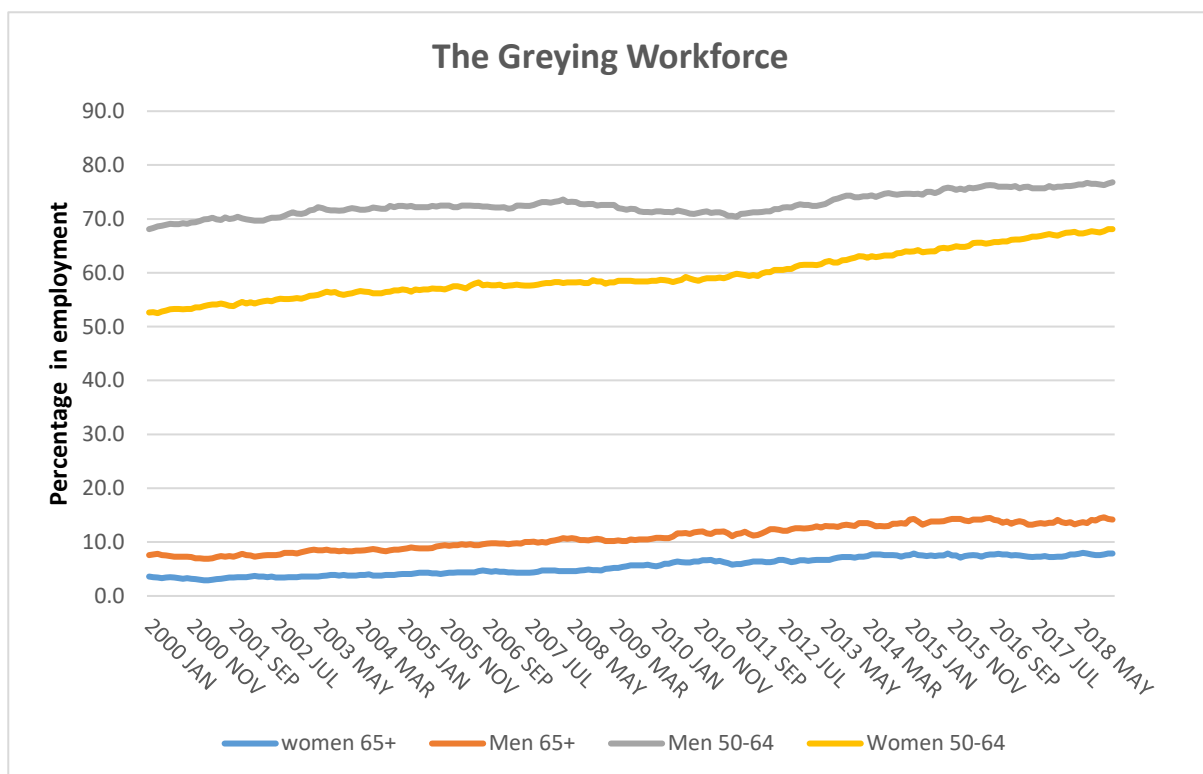
CLIENT NEWSLETTER – JUNE 2019

KEEP ON WORKING...?

What is the current state pension age (SPA)?

It sounds an easy question, but right now it is a moving target. If you answered 65, you are wrong because that stopped being the SPA last December. Until 6 October 2020 SPA is in a transitional period where there is no specific age, just a set of dates, each separated by two months, on which it arrives, depending upon date of birth. So, for example, if you were born between 6 February 1954 and 5 March 1954, you reach your SPA on 6 July 2019. From 6 October 2020 until 5 April 2026, SPA will remain at 66, before starting another two-year transitional period, en route to 67.

And the result is...



Source: National Statistics

The SPA has been on the rise since 2010, when the process of equalising state pension ages for men and women began. The effect of that controversial reform can already be seen in UK labour market statistics. In April 2010, at the start of the equalisation process, 58.5% of women aged between 50 and 64 were in the work. By January 2019 that proportion had risen to 68.1% - an increase of almost a sixth. As the graph shows, in that age band there are still proportionately more men in work, but the gap between the sexes has been narrowing since 2010.

Beyond 65, too

The trend of increased working life extends beyond age 65, as the two lower lines on the graph indicate. In January 2019, 7.9% of women aged 65 and over were still working, as were 14.2% of men. Many of the jobs involved are part-time.

The rise in SPA is not the only driver to the changing age profile of the workforce. Legislation that largely prohibits mandatory retirement ages has made it easier for employees to keep in harness. Tight labour markets – UK unemployment is under 4% – has encouraged employers to hang on to staff, on a full or part-time basis, rather than compete for new employees.

The income factor

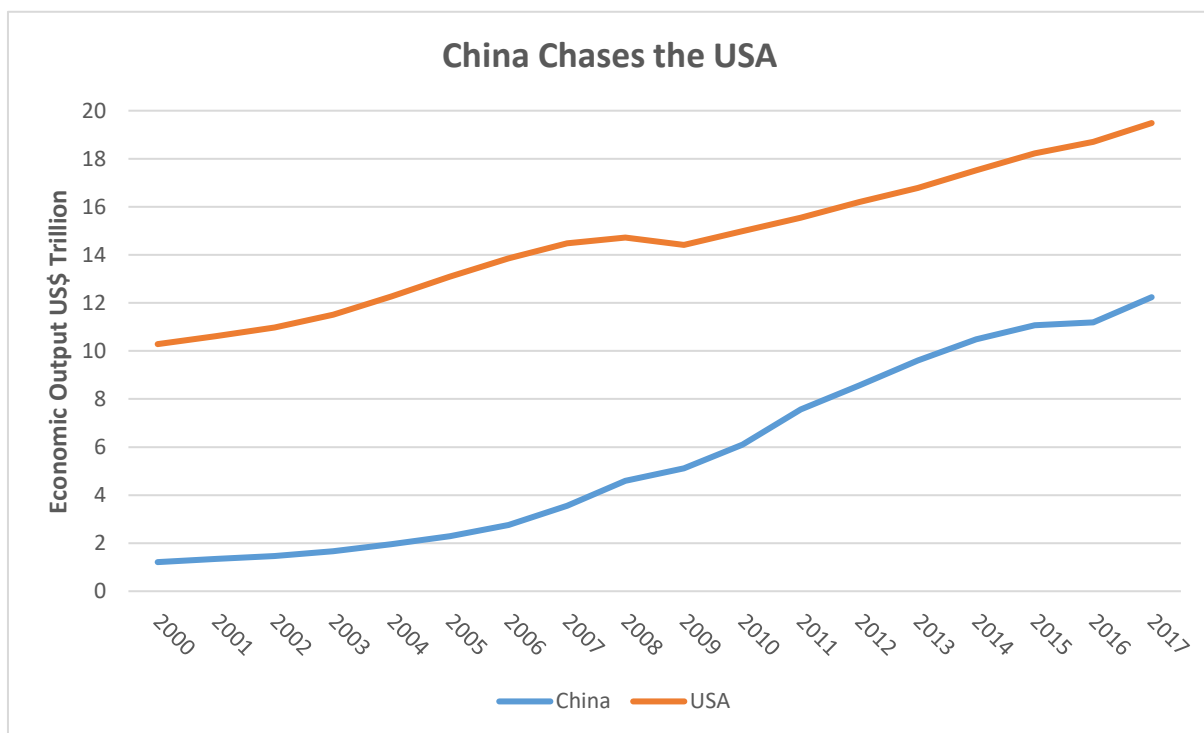
Probably the main reason for the growing grey-haired workforce is a financial one: they need the earnings. The state pension (theoretically £168.60 a week in 2019/20) hardly offers a comfortable retirement. Another factor is the gradual demise of final salary pension schemes, which most private sector employers have now closed to existing employees as well as new recruits. Such schemes often made it easier to take early retirement, especially if the employer added redundancy incentives. Workplace pension ages have also been rising too, often tracking the move in SPA.

ACTION

When you retire should be a decision you make, not a timing effectively set by the state or financial pressure. The only way to have that freedom of choice is to build up sufficient resources before you retire, by way of pensions and/or other investments.

Call us today for an analysis of when you can afford to retire, based on your current situation and level of retirement saving.

CHINA'S GROWING INVESTMENT IMPORTANCE



Source: World Bank

China has regularly been in the headlines of late. There has been the row over Huawei and its supply of 5G telephone equipment, the spread of Chinese international investment through its Belt and Road Initiative and the assorted trade disputes between China and the USA. The subtext to all these stories is the Middle Kingdom's rapidly growing economic and technological clout. China is already the world's second largest economy behind the USA. However, if the size of the two economies is adjusted for the relative purchasing power of the US Dollar and the Chinese Renminbi, then China has already reached the number one position. Politics dictate that neither the Chinese nor USA presidents mention this little-known fact.

Investment markets

China may officially be a communist country, but it has thriving stock markets that have a total value second only to those of the USA. Until quite recently, the Chinese share markets were largely closed to investors outside China, with foreign institutions having to operate via a quota system. As China has opened up, so too have its share markets and there are now links between the two big Chinese mainland stock exchanges, in Shenzhen and Shanghai, and Hong Kong which give non-Chinese investors access to Chinese-listed companies. A similar arrangement also came into being for fixed interest securities in July 2017.

Index providers react

The emergence of China from the investment shadows has affected the way in which professional investors view the country. Some major Chinese companies that have listed their shares outside mainland China, such as Alibaba and Tencent, already figure in many global portfolios and have found their way into stock market indices.

With increased access to Chinese mainland shares and improvements to Chinese corporate governance, the leading index providers, such as MSCI and FTSE Russell, are now adding Chinese mainland-listed shares to their indices. At this stage China is not being given its full weighting. In part this is to encourage further market and governance reforms within China. However, there is also the consideration that giving China its full weighting on day one would be extremely disruptive.

A good example is given by what is probably the most widely used index for emerging markets, the MSCI emerging markets index. In April 2019 that had a 5% weighting for Chinese mainland shares, representing just 0.8% of the total index. Were Chinese mainland shares given their full weighting, that figure would rise to 16.2%. A 15.4% reshuffle is no small thing when it is reckoned that the Index provides a benchmark for \$1,900bn of funds.

While the main focus has been on the Chinese share markets, China's fixed interest market is now being globalised in a similar way. At the start of April, Bloomberg started to include a limited number of Chinese fixed interest securities in its main global bond index. By November 2020, China will account for more than 6% of the index, which is still far from a full weighting, as China is the world's third largest bond market.

Is your portfolio turning Chinese?

The gradual inclusion of Chinese shares and bonds in major indices is proof that China is becoming a major investment territory. Institutional investors are increasing their exposure to China, if only because the indices against which they benchmark themselves are doing the same. The result is capital flowing out of other world markets and being reinvested in China. Those flows could push up the value of Chinese securities – hence the gradualist approach of the index providers.

ACTION

You may already have some Chinese investments if you have holdings in global or Asian funds. Whether or not that is the case, it is worth joining the index providers and reconsidering the importance of Chinese assets on the world investment stage.

Ask us to assess your portfolio's current exposure to China and the fund managers best equipped to handle a changing scenario for investment markets.

ISAs: START EARLY AND TAKE ADVICE

Have you forgotten ISAs, now the end of the tax year has passed?

Statistics from the Investment Association regularly show that ISA sales are clustered in the early months of the calendar year as investors react to a 5 April deadline. Look at the personal finance pages of the weekend press in March and it is hard to avoid all the ISA stories, including the journalist's favourite of ISA millionaires (they do exist). However, by mid-April ISAs seemingly go into hibernation. The puzzle is why that happens.

ISA benefits

ISAs offer some important tax benefits and, logically, to maximise their use, investment should be made at the *start* of the tax year, rather than its end. As a reminder:

- ISAs are free of UK income tax on dividends and interest;
- There is no UK capital gains tax on any profits within an ISA;
- There is nothing to report on a self-assessment tax return; and
- The tax benefits of an ISA can effectively be transferred to a surviving spouse or civil partner.

Take advice

Recent statistics issued by HMRC revealed that in 2017/18, 72% of ISA subscriptions were made to cash ISAs. While the cash ISA does have a role, you should give serious thought before using your ISA subscription to go down this route:

- Interest rates on offer are low. At the time of writing, only fixed term ISAs with terms of three years or more offered an interest rate above 2.0%.
- Over the years, many variable rate ISAs have moved from having relatively competitive rates to minimal rates as providers have launched new accounts to attract fresh money. Just because an account was called 'gold' does not mean it is not now closer to rusty iron.
- The personal savings allowance of up to £1,000 means that you may not need to use an ISA to earn tax-free interest.

Those low interest rates (CPI annual inflation was running at 1.9% in March 2019) have encouraged some investors to choose 'innovative finance' ISAs, which advertise higher returns. These are *not* cash ISAs and are outside the protection of the Financial Services Compensation Scheme. At the turn of the year one of the providers of such ISAs, which had been promoting 8% returns, went into administration. Subsequently HMRC decided that what had been marketed did not even meet ISA requirements, leaving investors not only with a capital loss, but also a potential tax bill.

ACTION

If you are planning to make an ISA investment in 2019/20, consider doing it now, rather than waiting for the March stampede.

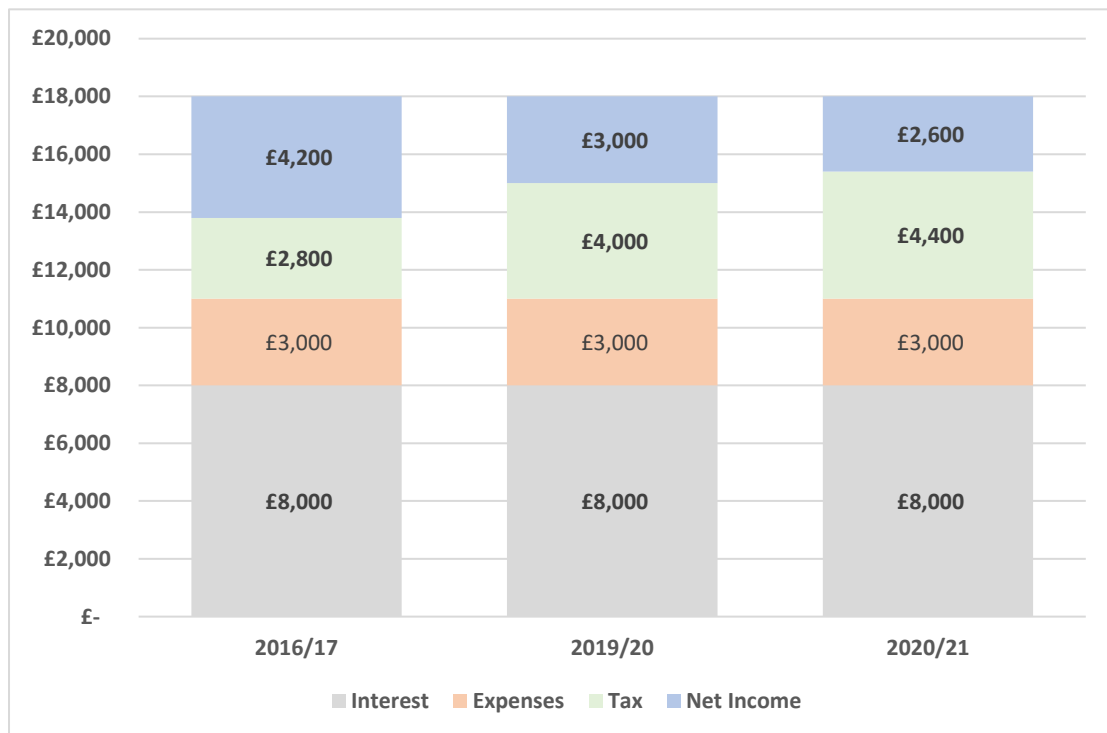
Call us today to discuss your ISA options and also to review your existing ISAs. What made sense a few years ago as an ISA strategy may not do so now.

RESIDENTIAL PROPERTY: MORE TAX CHANGES

6 April marked another change in the tax rules for residential buy-to-let (BTL) property owners. The new tax year 2019/20 saw the amount of interest on a BTL mortgage that can be set against rent cut from a half to a quarter, with a corresponding increase in the sum qualifying for a basic rate tax credit. From next tax year there will be no direct offset against rent and all interest will qualify for a 20% tax credit. That is bad news if you are BTL investor and a higher rate taxpayer, as the example below shows.

BTL Mortgage Interest Relief: A Costly Change

In 2016/17 Caroline owned a BTL residential property which produced rent of £18,000 a year. Interest on the mortgage she used to buy the property was £8,000 a year and expenses were £3,000 a year. If nothing else changes, as a higher rate taxpayer her net income will drop by 38% (£1,600) between 2016/17 and 2020/21. This £1,600 decline is due to the effective reduction in tax relief on her £8,000 interest bill from 40% to 20%.



And also in 2020/21...

Tax changes for residential property in 2020/21 are not limited to the final interest relief change:

- Any capital gains tax (CGT) on residential property will become payable within 30 days of a sale, if that occurs on or after 6 April 2020. The payment will need to be accompanied by an interim tax return.
- The period during which you can own two homes as main residences with neither of them being liable to CGT will be reduced in most circumstances from the current 18 months to just 9 months. In today's slow housing market, that could cause problems.
- Letting relief, which exempts up to £40,000 of gain from CGT if a main residence is let, will only apply if the owner remains in the property while it is let.

The unspoken government message

The various measures aimed at residential property in recent Budgets have the unspoken aim of making life easier for the first-time buyer and more taxing for the amateur residential property investor. Their effect is already visible in several ways, for example:

- A government survey of English private landlords published at the start of 2019 revealed that between 2010 and 2017 the proportion of landlords with just one rental property dropped from 78% to 45%. At the other end of the scale, the proportion of landlords with five or more properties – mostly professional investors - increased from 5% to 17%. They now account for almost half of all BTL properties.
- In 2018/19 the government's receipts from CGT increased by almost a fifth. Some commentators have suggested that the jump was at least partly due to small BTL investors selling up.

ACTION

If you own BTL property, make sure you understand how the current and future tax changes affect you and the net income you receive.

If you are considering selling up, talk to us about what can be done to mitigate any CGT bill and the reinvestment of the sale proceeds.

ANOTHER TAX YEAR, SAME OLD THRESHOLDS...

Once upon a distant time, the tax system was largely inflation-proofed. The default option was for allowances and tax bands to rise each year in line with RPI inflation. In theory Chancellors could overrule the automatic increases, but they were reluctant to do so unless they were grabbing the headlines with an above-inflation increase.

That rosy scenario started to change about ten years ago, when the financial crisis left the government hunting around for any means possible to raise extra revenue. Avoiding indexation was an easy way to increase taxes: keep the numbers unchanged and the Treasury silently reaps the benefits of inflation.

Nowhere is this more obvious than in the tax thresholds for three important components of the income tax system.

The £50,000 threshold

Once your (or your spouse's/partner's) adjusted net income (broadly total income with minor adjustments, eg for Gift Aid) exceeds £50,000, the High Income Child Benefit Charge (HICBC) is triggered. This is a tax levied at the rate of 1% of Child Benefit paid per £100 of income over the £50,000 threshold. When the HICBC was introduced in 2013, the higher rate tax threshold was £42,475; the two are now identical, other than in Scotland.

The £100,000 threshold

At an adjusted net income level of £100,000, the phasing out of the personal allowance begins at the rate of £1 for each £2 above the threshold. Thus, with a personal allowance of £12,500 in 2019/20, all personal allowance is lost if income is £125,000 or more. The £100,000 point has been unchanged since it was first announced by Alastair Darling (remember him?) in 2009.

The £150,000 threshold

The starting point for additional rate tax was also set 10 years ago by a Labour Chancellor and has subsequently been untouched by his Conservative successors. It provides a classic example of the stealth tax effect of frozen thresholds. In the first tax year additional rate applied (2010/11), 236,000 people were caught, whereas by 2018/19 393,000 were paying the top rate of tax – an increase of two thirds.

ACTION

The frozen thresholds can catch you unaware as a small rise in income – perhaps a promotion – can click the trigger. This has particularly been the case with the High Income Child Benefit Charge, the impact of which HMRC has now accepted was not adequately explained in 2013. At this stage in the tax year it is worth estimating what your total income in 2019/20 will be, so that you are aware which thresholds you might be crossing.

The fact that the thresholds are fixed – and therefore reducing in real (inflation-adjusted) terms each year can make them difficult to avoid. However, there are a range of proven strategies which can be used to mitigate the effects, even if the trigger point cannot be avoided. If you have been caught by any of these frozen thresholds, do ask us to outline what could work in your circumstances.

Past performance is not a reliable guide to the future. The value of investments and the income from them can go down as well as up. The value of tax reliefs depend upon individual circumstances and tax rules may change. The FCA does not regulate tax advice. This newsletter is provided strictly for general consideration only and is based on our understanding of law and HM Revenue & Customs practice as at June 2019. No action must be taken or refrained from based on its contents alone. Accordingly no responsibility can be assumed for any loss occasioned in connection with the content hereof and any such action or inaction. Professional advice is necessary for every case.