

Newsletter July 2021

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2021: six months down...

The first six months of 2021 have been rewarding for investors, but the next six are uncertain.

Index	H1 2021 Change
FTSE 100	+8.93%
FTSE All-Share	+9.21%
Dow Jones Industrial	+12.73%
Standard & Poor's 500	+14.41%
Nikkei 225	+4.91%
Euro Stoxx 50 (€)	+14.40%
Shanghai Composite	+3.40%
MSCI Emerging Markets (£)	+5.34%

Source: FTSE.

The first half of 2021 was a much less traumatic ride for investors than the first half of 2020. With hindsight, last November's Pfizer/BioNTech vaccine breakthrough announcement gave investment markets a fresh momentum that continued through the first two quarters of 2021, particularly in the US.

However, the drivers of performance have somewhat changed in the past 12 months. Last year was the year of technology stocks, with the likes of Apple, Microsoft and Amazon leading the way. In 2021, that has not been the case, even though the top five technology stocks account for more than 21% of the S&P 500 index value. Research by Bloomberg shows that in the first half of 2021, information technology (IT) was a drag on the S&P 500. Strip out IT from the index and it would have risen by 14.9%, not 14.4%. Alternatively, give each share in the index an equal weighting – so those top five companies become just 1% of the index – and performance over the first half would have been 18.3%.

The cooling of US tech stocks helps to explain why the Eurozone, as measured by the Euro Stoxx 50, matched the S&P 500 in the first six months of the year. Even that is not the whole picture though, as the dollar strengthened by about 2.5% against the euro over the period, leaving the US market the winner in currency-adjusted terms. Most indices are based on the relevant domestic currency, with currency-adjusted versions largely the domain of professional investors.

Will 2021 now prove to be the proverbial game of two halves? There are two obvious uncertainties ahead:

- During the first half of this year, inflation was on the rise globally. The worst/best example is the US where CPI inflation was 1.4% last December but rose to 5% in May. At present, the consensus view is that this inflationary jump is 'transitory'. By next January, we will have a good idea whether that is the right judgement. If it is not, interest rates could rise – something the markets would not welcome. If it is correct, rate rises will likely remain distant and markets happy.
- The pandemic is not yet over, especially outside the developed world. Covid-19 has already surprised in a variety of ways and could do so again – for good or bad.

The first half of 2021 showed how markets change underneath the headline numbers. To benefit from such movements, professional investment management is vital.

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Investing in shares should be regarded as a long-term investment and should fit in with your overall attitude to risk and financial circumstances.

What is an adequate retirement income?

A leading pension think tank has examined this question – but the findings aren't straightforward.

Over the years, there has been much focus on the tax treatment of pensions and ways to encourage greater saving for retirement. Arguably, there has been less attention paid to the question of how much income you will need once work ceases.

The Pension Policy Institute (PPI) recently published a paper examining what an adequate retirement income means today in dollar terms. The paper notes that the last serious effort to address the issue was undertaken by the Pensions Commission nearly two decades ago, leading eventually to the introduction of automatic enrolment. The PPI makes the following points:

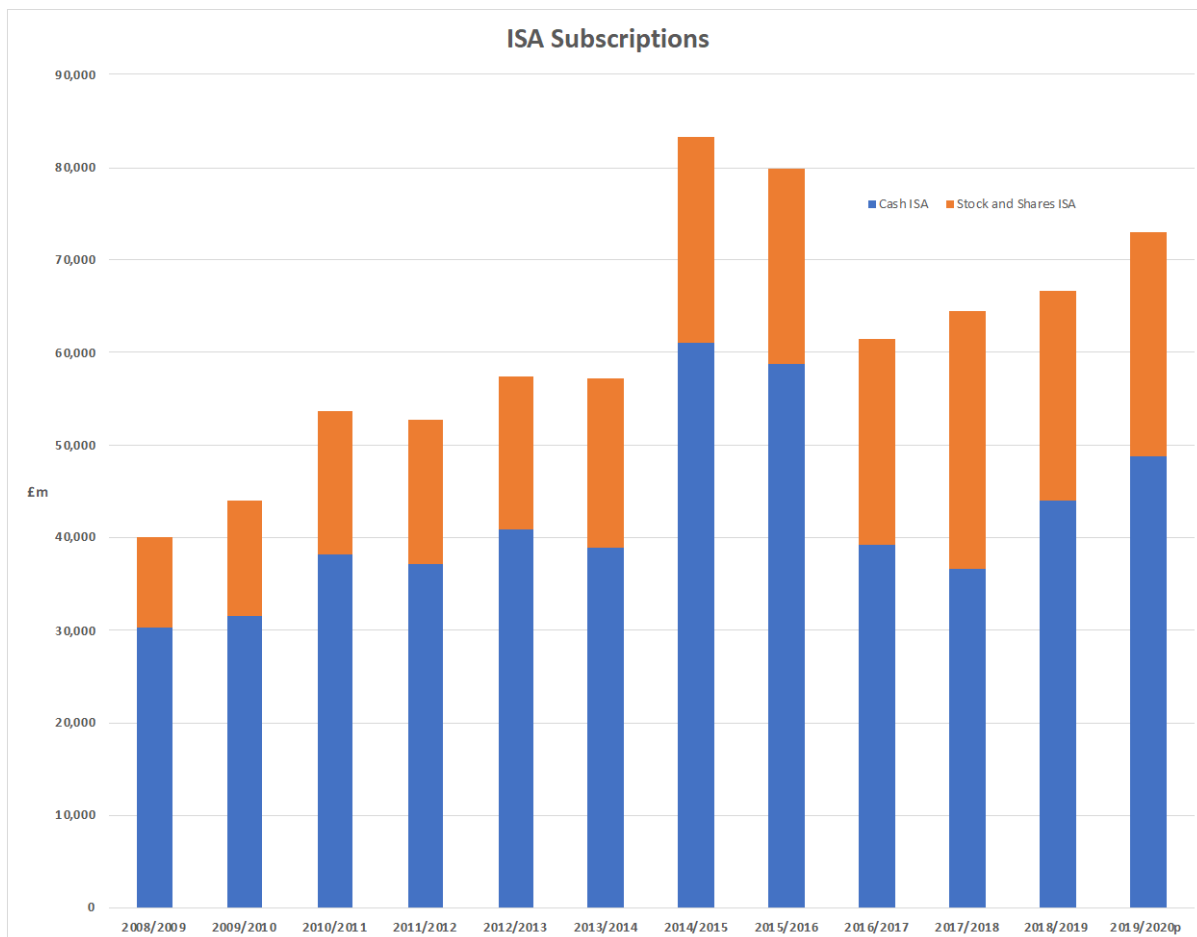
- Individuals, employers, the state and society generally all have differing views on what constitutes adequacy. For example, the state view is set by the Guarantee Credit element of Pension Credit (£177.10 a week for a single person and £270.30 for a couple).
- Changes to the pensions landscape since 2000 have altered the retirement picture both positively and negatively. For example, the new state pension is higher than its basic state pension predecessor, but state pension age has increased (to 66 for men and women) and will continue to increase.
- The demands made on assets originally saved to provide a retirement income have increased, for example:
 - For some people, there is a widening gap between leaving work and receiving their state pension, a situation exacerbated by pandemic-prompted early retirements;
 - More often now debts, including mortgages, will be carried over into retirement;
 - The shrinking of home ownership will see more retirees having to pay rent; and
 - There may be a need to support other family members – the Bank of Mum and Dad may not be able to close at retirement.
- The traditional emphasis on retirement *income* ignores the need to deal with 'personal financial shocks', which are better addressed by considering retirement *capital*.

The PPI says that many people make their retirement planning decisions 'without support'. It goes on to warn that "As a result, many people struggle to make pensions and savings decisions which offer them the best chance of both achieving their aspirations for retirement and protecting themselves against future risk." Don't let that be you – talk to us about assessing what an adequate retirement income means for you and how it can be achieved.

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The wrong type of ISA?

New statistics from HMRC show over £300bn invested in cash ISAs.



Source: HMRC.

One of the many knock-on effects of the pandemic has been that HMRC's annual updating of statistics has suffered delays. As a result, details of ISA subscriptions and holdings for 2019/20 have only just emerged. Among many interesting facts, the data shows:

- Despite ultra-low interest rates, the amount of money invested in cash ISAs has continued to grow. In 2019/20, £48.75 billion of subscriptions were received, more than twice as much as was invested in stocks and shares ISAs.
- The increase in the maximum overall ISA contribution to £20,000 in 2017/18 (from £15,240) has still not driven total annual subscriptions above their 2014/15 peak.

- Lifetime ISAs (LISAs), launched in 2017/18 to no great fanfare, have since grown in popularity, with 2019/20 subscriptions more than double those of the previous year. This jump may have been helped by the closure to new investors of the Help to Buy ISA in December 2019.
- For the first time, over one million subscriptions were made to Junior ISAs (JISAs) in 2019/20, with total investment of £974 million.
- The total amount invested in ISAs (excluding JISAs) in April 2020 was just under £620 billion, of which just over half was held in cash ISAs. The cash proportion would likely be substantially smaller today, as the value of stocks and shares ISAs were depressed in April 2020 when the first lockdowns got underway.

The continued dominance of cash ISAs is, at least in part, a reflection of the lack of financial planning advice received by many ISA investors. The personal savings allowance, introduced in 2016/17, means that basic rate taxpayers (calculated using UK-wide rates) pay no tax on their first £1,000 of interest and, similarly, £500 of interest is tax free for higher rate taxpayers.

At current interest rates, it takes a considerable amount of capital to exceed even the lower threshold so taking out a cash ISA could be of questionable value compared with an ordinary deposit, which might pay a higher interest rate. However, the ISA framework could be useful to you in other ways, so advice is essential before taking any action on a cash ISA.

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The £9 billion Child Trust Funds backwater

Over £9 billion was invested in Child Trust Funds (CTFs) as of April 2020, according to new HMRC data.

If you have a child or grandchild born between 1 September 2002 and 2 January 2011, they were almost certainly the beneficiary of a government payment – either £250 or £500 – into a CTF. The theory behind the CTF scheme was to ensure every child had some savings as they entered adulthood.

In practice, the scheme was not a great success. Nearly a third of parents ignored the CTF vouchers they received, leaving HMRC to open default CTFs from accredited providers chosen

at random. The scheme survived until 2010, when the new coalition government cut payments dramatically and subsequently closed it entirely from the start of the following year. By then, there were over six million CTFs in existence.

HMRC recently published some limited data on CTFs, which revealed:

- In April 2020, shortly before the first CTFs started to mature, there was nearly £9.2 billion invested in CTFs, with the average CTF having a value of £1,500.
- Over 85% of CTFs had a value of less than £2,500. Strangely, HMRC did not give any more detailed breakdown of these sub-£2,500 CTFs, but some detective work suggests that their average value is below £1,000.
- CTFs were not limited to receiving government payments and the option for top-ups remains to this day, with a current maximum of £9,000 in a tax year. However, in 2019/20, fewer than one in six plans were topped up, with the average addition being £430.

The data paints a picture of most CTFs as small, receiving no new monies and being potentially forgotten. The government tacitly acknowledges this. As part of its package for dealing with the steady flow of maturing CTFs, it launched a find-a-CTF website (<https://www.gov.uk/child-trust-funds/find-a-child-trust-fund>).

If your child or grandchild has a CTF, it makes sense to review it now to ensure they don't miss out. Since April 2015, it has been possible to transfer a CTF to a Junior ISA (JISA) but not vice versa – a child can only have the one or the other. Often, a new JISA will offer much wider investment choice than the old CTF and may have lower charges.

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The Triple Lock trip up, take two

State pension increases and the Triple Lock are back in the spotlight.

About a year ago, during the first wave of the pandemic, several think tanks started to look at the potential repercussions of the then crumbling economy on state pensions. Their particular focus was on the 'Triple Lock', which applies only to payments made under the old basic state pension and its replacement, the new state pension.

As a reminder, the Triple Lock means that these two state pensions increase in April by the greater of one of three measures:

- Yearly CPI inflation to the previous September;
- Average weekly earnings growth measured over three months to the previous July; and
- 2.5%.

At the time, the economists' best guess was that the hit to earnings caused by Covid-19 in 2020 would be followed by a V-shaped recovery in the following year. The result that concerned the think tanks was that:

- In April 2021, the Triple Lock would mean state pensions rose by 2.5%, sidestepping a fall in earnings and minimal inflation; and then
- In April 2022, the recovery in earnings would mean that under the Triple Lock, state pensions growth matched earnings growth, well above 2.5% or inflation.

Speculation suggested that the Chancellor would have to act to limit the cost to the Exchequer, despite a 2019 Conservative manifesto pledge to retain the Triple Lock. In the event, the only action the government took was a tweaking of legislation to ensure the Triple Lock would continue to operate for the 2021 increase.

As we near the time when the 2022 increases are published, the number crunchers have returned to their spreadsheets. With the benefit of more hard data, some are now estimating that an unaltered Triple Lock could deliver an 8% rise next April, costing the Chancellor £4 billion.

This subject is certain to gain more attention once summer ends and pre-Budget rumours take off. However, even if an 8% rise does come to pass, the new state pension will still be less than £200 a week. **B** So, you will still need to keep making your own pension contributions...

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