Essential FINANCE

Issue 16 / Summer 2021 | Eastwood Financial Services Ltd

The last time I wrote this note, I finished it with a hope of warmer weather to come!

Well we certainly got that didn't we?! Possibly a little bit too warm really but as I write this from my garden on a sunny Sunday afternoon, the heat is a lot more bearable.

So what's been going on with us since the last time I wrote?

Well, we've welcomed three more new recruits and our resident wildlife photographer Tim has continued to work his magic… as you'll see on our news pages. Becky Brooke has also returned from her maternity leave and we are all enjoying watch her lovely little girl Willow change and develop.

We are also starting to see our team take well deserved holidays over the Summer. It was a little on the quiet side last Summer with people not really taking time off to go away on holiday but they are all starting to do so again now, which is nice to see. I've just returned myself from a lovely short break in Rye, East Sussex and am feeling very lucky to have a holiday in Cornwall booked in for later in the year.

This quarter's edition has very much an investment and tax theme to it… I think I'd struggle to pick a favourite article this month… they are all of equal interest. We've borrowed the article on luxury watches from our sister company Eastwood Private Clients (courtesy of Doerr Dallas Valuations) and we hope you find this as fascinating as we did.

As always, we hope you find this edition of interest and if there's anything that you'd like to discuss in more detail, please do not hesitate to contact us.

By the time I write again, the coolness and beautiful colours of Autumn will be upon us. But in the meantime, enjoy the rest of the Summer… I'm signing off now to treat myself to a lovely cold glass of rosé wine. Well it is a sunny Sunday afternoon after all!

With best wishes from myself and all of the team,

Karen

Karen Wynard DipPFS
Managing Director

This newsletter is for general information only and is not intended to be advice to any specific person. You are recommended to seek competent professional advice before taking or refraining from taking any action on the basis of the contents of this publication. The Financial Conduct Authority does not regulate tax advice, so it is outside the investment protection rules of the Financial Services and Markets Act and the Financial Services Compensation Scheme. The newsletter represents our understanding of law and HM Revenue & Customs practice.

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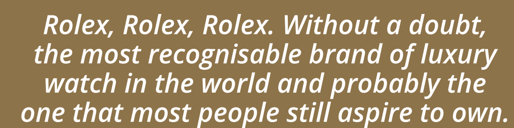

Is the smart money still in luxury watches?

It's a question that is asked of our specialists by all our high net worth clients who have wristwatch collections.

Whether its a few 'accidental' investments or hardened collectors who purchase an item to open the box and admire the marvel of what they have in front of them... and then hide it away in a safe never to be seen again, the question of whether the smart money is still in luxury watches remains.

That is, until they need it to be valued or to provide proof to their authorised dealer that their name should be top of the list for that new GMT that us mere mortals have to wait more than a decade to get hold of.

As with most things of this nature, it is not an easy answer. If I were to ask one of my extremely learned colleagues "is the smart money still in art?" then the ensuing conversation could probably last hours, would definitely involve strong language, and ultimately would end with everyone having a subjectively correct answer.

Whilst we cannot predict the future, if the last decade has been anything to go by (including 18 months of complete global turbulence) the market has been strong beyond any comprehension that us watch enthusiasts could have possibly thought about 20 years ago.

Rolex, Rolex, Rolex. Without a doubt, the most recognisable brand of luxury watch in the world and probably the one that most people still aspire to own. Their marketing is exemplary, their product line is still world beating in many areas and owning one still makes you feel special... but, the problem is actually owning one.

If you have mustered the courage to enter into one of their boutiques to actually try on some of their timepieces, you will notice that you are being visually credit scored by both the assistant and security guard making sure that you really should be in here.

But when you finally see that 'Submariner' that you have dreamt of since seeing Timothy Dalton in Licence to Kill (Insert Connery & Dr No as required) you know it was all worthwhile, but just as you reach for your wallet, the blood drains from your face and you feel like Patrick Bateman trying to book a table at Dorsia.

You cannot buy a brand new Rolex Submariner. Really. Seriously. We could talk about examples such as the 'Pepsi', 'Coke', 'Kermit', and 'Starbucks' models and show even larger increases in value, however this should give an overview on why your clients need to have their watches valued on a regular basis, and it's not just Rolex – Patek Phillipe and Audemars Piguet, many other high end brands command eye watering prices on the secondary market.

For instance, the GMT Master II 'Batman' had a brand new retail price of £7,750 and the secondary market price reached up to £17,000. Likewise, the Submariner (no date 41mm) had a brand new retail price of £6,450 and a secondary market price of up to £12,495. We also saw that the Daytona Cosmograph (40mm Oystersteel) had a brand new retail price of £10,500 and a secondary market price of £25,000... so is the smart money still in luxury watches? We shall leave you to decide!

Courtesy of Doerr Dallas Valuations

Article taken from the 'Exclusive' newsletter of our sister company Eastwood Private Clients, and is provided courtesy of Doerr Dallas Valuations.

Please note that this article has been included only for the purpose of general interest – Eastwood Financial Services are unable to provide any advice or guidance on this subject.

Handling high markets

Most of the world's major stock markets are at or close to their all-time highs, but that is not necessarily a reason to stop investing.

Global stock markets have been performing strongly since the first successful vaccine trials in November 2020. Anticipation – and evidence – of economic recovery has prompted share prices to rally around the world. In the world's largest market, the US, the S&P 500 Index breached the 4,000 level for the first time ever, following a drop to below 2,500 in March 2020 when the pandemic panic was at its worst. Even the UK, which has lagged behind in recent years, has picked up, with the FTSE 100 index crossing the 7,000 barrier again.

Inevitably, the flow of "...hits new high" headlines has prompted questions about the wisdom of investing in share markets *now*. Neither of the obvious alternatives of cash deposits or fixed interest securities are particularly attractive, given current ultra-low interest rates. However, if you have similar market doubts, there are several strategies to consider:

- **Drip feeding** Instead of investing a lump sum all at once, spread the investment over a period. That way you can be sure all your money does not get invested at a market peak. The corollary is that you may miss out on some investment return if markets continue their upward path.
- **Keep an adequate cash reserve** Make sure you have sufficient instant access deposits so you can avoid cashing in your investments if you need funds quickly. A paper loss is just that until investments are realised – as events since February 2020 have amply demonstrated.
- **Be aware of sequencing risk** If you intend to draw on your investment immediately, as might be the case with pension drawdown, a sudden drop in values can have a dramatic effect on the sustainability of your withdrawals. There are several approaches to limit this risk, such as holding a separate low risk reserve.

For more information on these and other high market strategies tailored to your personal circumstances, please contact us.

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The future of inheritance tax

Most over 55s have no idea whether there might be inheritance tax (IHT) to pay on their estate — or what the liability might be. With change on its way, understanding IHT may be more important now than ever.

The £325,000 IHT threshold (or £650,000 for married couples and civil partners) has remained unchanged since 2009. The Budget 2021 freeze on this nil rate band until 2025/26 means that many more estates could be subject to IHT, as inflation – particularly of house prices – pushes up many people's total net worth.

IHT is generally charged at 40% on the value of assets over the threshold. There are exemptions, the most significant being assets left to a spouse or civil partner. These transfers are normally free of IHT, regardless of their value. In addition, if parents leave a home to children or grandchildren the threshold increases to £500,000 using the residential nil rate band of £175,000. For married couples and civil partners this effectively means an estate of up to £1 million can be left to their children tax free.

Simple steps to reduce IHT

You can give away money or other assets during your lifetime. But it has to be a genuine transfer – giving away a property while continuing to live in it wouldn't count.

- **Small gifts** You can make unlimited gifts of up to £250 per recipient during the tax year, plus up to £3,000 per tax year — as one gift or multiple gifts – under the 'annual exemption' rule. None of these gifts are included within your estate for IHT purposes.
- **Exempted gifts** Further gifts are permitted each year for specific reasons, e.g. £5,000 or £2,500 towards a child's or a grandchild's wedding; or payments to help with an elderly parent or a child's (under 18) living costs.
- **Larger gifts** If you give away more than £325,000 in the seven years before your death, these gifts may be subject to IHT. If you survive three years or more after making a non-exempt gift, taper relief reduces the tax payable on a sliding scale and no tax is payable if you survive seven full years following the date of the gift.

Potential reform

Significant changes to IHT may be on the horizon. Last year an All-Party Parliamentary Group made a series of recommendations including a 10% tax rate on lifetime gifts over £30,000 per year, 10% on gifts on death up to £2 million and possibly 20% thereafter.

Meanwhile the Office of Tax Simplification (OTS) has also published recommended reforms including:

- *Exemptions* The three main exemptions – the £3,000 annual exemption (frozen since 1981), the £250 small gifts exemption (frozen since 1980) and the normal expenditure exemption (with no monetary limit), together with marriage gifts (frozen since 1975) – should be consolidated into a single annual gift allowance. The OTS did not specify an amount but noted that £25,000 would cover just over half of all normal expenditure claims.
- *Business relief* IHT business relief and capital gains tax (CGT) uplift on death can mean business assets pass with no IHT and no CGT, if sold immediately. The OTS proposed ending the CGT uplift, but the Chancellor might take a different view, given the growing popularity of certain portfolios (including ISAs) tailored to benefit from business relief.

Put plans in place

While the future shape of IHT is uncertain, the tax itself is unlikely to disappear. You should not defer IHT planning – which should be interwoven with your will and other estate planning – waiting for changes that may not happen. If IHT is a concern for you, the time to talk to us is now, especially as any reform could see the removal of some opportunities.

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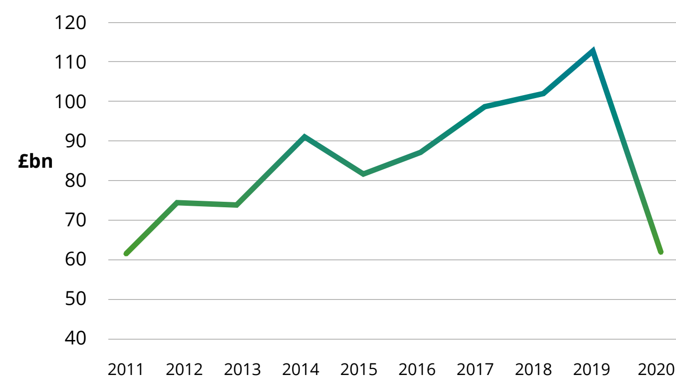
Dividends recover in 2021

Last year many companies were forced to cut or suspend dividend payments. This year, the reverse is happening and dividends are generally on the up.

UK Total Dividend Payments 2011-2020



Source: Link Asset Services

Many income-seeking investors would prefer to forget 2020. Global interest rates stayed around zero (or below), while many companies throughout the world cut or suspended their dividend payments. The average fall in global dividends in 2020 was 12.2%, according to one leading international investment manager. However, the global picture is distorted by the resilient performance of North America, which saw a small rise in dividends. Strip out North America from the world data and the picture elsewhere was mostly grim.

Dividend cuts were particularly prevalent in the UK, as the graph shows. Between 2019 and 2020 the total value of dividends (regular and one-off) paid by UK companies fell by 43.1%. Most of that reflected the decline in regular dividends, although proportionately there was a much greater fall in one-off payments. From April 2020 to December 2020, nearly a third of UK companies cancelled their dividends, while close to another quarter cut them.

In some instances, the companies had no other option. The main UK banks were effectively ordered by the Bank of England to end dividend payments as a way of preserving their capital. Others, such as airlines, had little choice because their revenue disappeared. There were also businesses that took the opportunity presented by the pandemic to make overdue adjustments to how much profit they passed out to shareholders. Arguably, the 'rebasing' of dividends by the UK's two oil majors, BP and Shell, was an example of this pragmatism.

Looking up in 2021

In 2021, the clouds seem to be lifting. The banks have been allowed to resume dividend payments, although at a lower level than in 2019. Some companies that suspended dividends as a precaution have begun making payments again. Even Shell, which cut its quarterly dividend from 47¢ to 16¢ in June 2020, has started to increase its quarterly payments.

Inevitably, there are companies in sectors such as hospitality and retail that continue to conserve cash, but these should benefit from the bounce back that is emerging in economic activity.

Link Asset Services, one of the largest share registrars in the UK, has estimated that in its best-case scenario, regular dividend payments will rise 5.6% in 2021. Its worst-case scenario is still positive, with dividends rising by just 0.9%. Link says that "companies are increasingly declaring dividends in line with our best-case scenario as the economy comes back to life and constraints on pay-outs are lifted".

Should you wish to discuss this matter in more detail, please do not hesitate to contact us.

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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.

Coming in from the cold: tax planning for families

The freezing of many tax thresholds and allowances has increased the importance of family tax planning.

In his spring 2021 Budget, the Chancellor announced that the following thresholds and bands will not change until April 2026:

- The personal allowance – £12,570;
- The higher rate threshold – £50,270 outside Scotland;
- The capital gains tax annual exempt amount – £12,300;
- The standard pension lifetime allowance – £1,073,100; and
- The inheritance tax nil rate band (£325,000) and residence nil rate band (£175,000).

The Chancellor said nothing about the many other tax thresholds and limits that are not subject to automatic inflation-linking. For example, the starting point for additional rate tax has been £150,000 since it first appeared in 2010/11.

This form of stealth tax is favoured not only by Mr Sunak, but also appealed to many of his predecessors. Unless inflation falls to zero – and the forecast is for prices to rise faster in the short term – such freezes mean that more people become taxpayers and those who are already taxpayers will pay more tax. The government estimates that by 2025/26 it expects 1.3 million more people to be paying income tax and one million more to be higher rate taxpayers than would have been the case if the tax thresholds were inflation linked.

The eroding effect of these freezes means that many couples who have not had to think about their tax planning *jointly* now need to do so. For example:

- *The high income child benefit charge* only applies if one or either of a child's parents, or adults in the child's household (married or not), has income exceeding £50,000 – a figure unchanged since January 2013. When combined with higher rate tax, the result is a marginal tax rate of up to 58.3% (59.3% in Scotland) for a two-child family. By rearranging ownership of their investments – and hence receipt of investment income – some couples may be able to avoid either of them reaching the £50,000 trigger point.
- *Charitable gifts* that qualify for gift aid automatically receive basic rate relief at source, meaning that an £80 net gift is worth £100 to the receiving charity. What many people don't know is that higher and additional rate taxpayers can claim extra personal tax relief. For instance, a higher rate taxpayer can claim £20 relief (£21 in Scotland) on the same £80 net gift. Couples making joint decisions about charitable donations therefore need to decide who should make the gift.
- *Capital gains and capital losses for married couples and civil partners* You each have a capital gains tax (CGT) annual allowance of £12,300. If you make a capital gain of £15,300 in a tax year and your partner makes a loss of £3,000, you end up with a CGT charge on that loss, even though your joint net gains match the annual exemption. On the other hand, if your partner transferred their loss-making asset to you and then you sold it, the loss could offset your gain.

Relationship status matters

As with any area of tax planning, make sure you take advice before acting. For instance, the capital gains tax example above will not work for couples that are neither married nor civil partners – the transfer of shares would crystallise the loss.

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The importance of portfolio rebalancing

Inertia can be a dangerous trait, especially for investment.

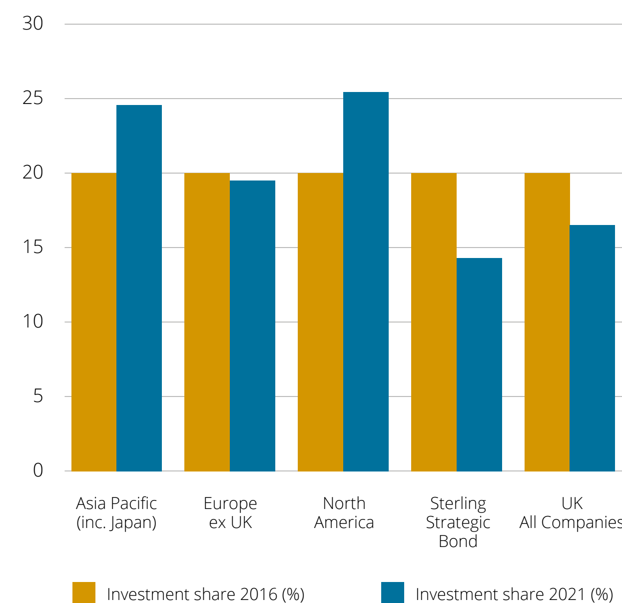
You know the feeling. Sometimes it just seems easier to leave things as they are for another year rather than take any action. Call it the 'If it ain't broke don't fix it' syndrome. But putting things off risks costly problems that could be avoided with regular maintenance.

As it is with central heating boilers, so it is with investment. A portfolio created several years ago can alter over time without the changes being obvious. The names on the investment will generally be the same, as will your share/unit holdings, but much may have happened underneath:

- Different sectors and different global markets will have performed differently. That is why diversification is so often highlighted as important: you do not want all your eggs in one basket.
- The relative importance of markets or sectors may have changed. A classic example is China, which has risen from being just another emerging market to becoming the third largest global stock market after the US and Japan.
- Funds may have changed ownership, manager and/or investment approach, but still retain the same name.

Unmanaged funds drift

As an example, imagine a portfolio split equally across five major investment sectors that was established on 30 April 2016. Each holding would account for 20% of the total. Five years later, based on the average performance for each of the sectors, the picture is rather different as illustrated in the chart below:



The North America sector (basically the US) is now 25.5% of the portfolio, while the Sterling Strategic Bond has shrunk to 14.4% and the UK All Companies to 16.5%. The overall result is a less diversified portfolio with 69.1% in overseas share markets against 60% in 2016.

If the portfolio had been reviewed and rebalanced each year, it would not have drifted so far from its starting point. That is the penalty for investment inertia and why we recommend regular reviews, even if the result in some years is 'no change'.

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Responsible investing and 'greenwashing'

There has been huge growth in the number of 'sustainable' and 'responsible investment' funds, which now look at a company's environmental, social and governance (ESG) track record as part of the investment process. However not every 'green' label should be taken at face value.

In some cases these terms are simply being used as a marketing tool — a trend known as 'greenwashing'. Investors might assume they are in a climate-friendly fund, but the reality could be quite different.

MPs are now calling on regulators to do more to address this issue and more widely there is a growing push for European regulators to police how the fund management industry reports ESG issues.

It is likely to be some time before there is regulation on this issue. Until then, investors will need to take a closer look at funds. This process isn't always easy and is complicated by the raft of financial and technical jargon used.

To select a fund that is aligned to your values it's worth considering the following issues.

- *Active or passive:* Passive funds may have limited ability to exclude stocks, but there are specialist indices weighted on carbon emissions as well as the FTSE4Good indices.
- *Top ten holdings:* Most funds publish their ten biggest holdings on fact sheets, giving an indication of where your money is invested.
- *Commitments and pledges:* There are numerous organisations working with the financial industry to address climate change, such as Make My Money Matter, Climate Action 100+ and the Net Zero Asset Managers Initiative. Check whether a fund manager has signed up to the aims of one or more of these organisations. For guidance on making your investments more sustainable please get in touch.

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The rise of second homes

The number of people purchasing second properties in the UK has boomed according to government figures, with the total number of second homes rising by 30% over the past five years.

The recent Stamp Duty holiday has further increased activity in the housing market, as many people look to benefit from this short-term tax concession.

Second home-owners include those buying properties to rent out, either as short-term holiday lets or on longer-term rental contracts to tenants, as well as those buying a property solely for their own use. Many will do a bit of both: using a second property for weekends away, while also letting it to friends, family and also commercially for some of the year to help cover costs. However, this can affect how much tax you need to pay on any income the property generates.

Homes that are classed as a 'furnished holiday let' (FHL) benefit from several extra tax breaks. For example, owners can deduct as expenses the cost of furnishing the property and mortgage interest charges. Income from FHLs can be used to make pension contributions, which is not permitted for income from buy-to-let property. There are several rules for a property to qualify: for example, it must be available for letting at a commercial rate for at least 210 days a year and it must not normally be let to the same person for a period of more than 31 days in the tax year.

If you are renting out a second property, you should seek qualified tax advice to ensure you make the most of the rules.

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Your home may be repossessed if you do not keep up repayments on a mortgage or other loans secured on it. Business buy-to-let and commercial mortgages are not regulated by the FCA. Think carefully before securing other debts against your home.

Track down lost assets

Up to £15 billion is believed to be sitting in 'lost' savings accounts, premium bonds and pension and investment accounts.

Many people lose track of accounts when they move house, misplace statements or even change computer and forget to update their login details. Tracing these assets can be complicated, particularly after banks or investment companies merge or rebrand.

Share, record, research

Even if you have kept a meticulous record of your finances, it's important to make sure family members know how to access them. Recent research suggests that one in seven people take hidden assets to the grave, as family members don't know about long-lost savings accounts.

Avoid your hard-earned savings getting lost by updating your will, making sure executors have a copy of all financial accounts — or nominate a charity for some of these funds.

To track down lost accounts contact **mylostaccount.org.uk** – an online portal that traces old bank, building society, and NS&I accounts.

Financial News Round Up

Rates on the rise…

Although the Bank of England's base rate has been 0.1% for over a year, other interest rates have been on the move. Most notably, yields on long-term government bonds have more than doubled. That is good news if you are nearing retirement and thinking about a pension annuity, as rates have risen.

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Minimum pension age

The government has confirmed that the normal minimum pension age, the earliest age at which private pension benefits can normally be drawn, will increase from the current 55 to 57 from 6 April 2028. The timing coincides with the end of the next phased increase in State Pension Age from 66 to 67.

Make sure your retirement plans are flexible

Nearly two in five people brought their retirement age forward in the past year, according to a recent survey of those retiring in 2021. It's a salutary reminder of the importance of building flexibility into your retirement plans.

EFS News

Garden Wildlife

At the beginning of the first lockdown, Tim Ball, our Chartered Financial Planner and wildlife photographer, decided to set up a wildlife camera trap in his garden, mainly to see if he had any hedgehogs visiting.

Throughout the year Tim has had red foxes visiting on a daily basis, but a couple of weeks ago Tim found out he also has had a badger making an appearance too, which he was really excited about.

Badgers are short, stout, powerful animals that live in underground 'setts' and these can be as large as over 50 metres long! They are members of the mustelid family, which also includes pine martens, otters, polecats, ferrets. Badgers are omnivores, which means they will eat a wide range of food. Most of (around 80%) of a badger's diet is made up of earthworms – they can eat hundreds of them in a single night – but they also eat slugs and other invertebrates.

Welcome Back Becky!

Our Administrator Becky Brooke returned to work in May after welcoming her daughter Willow to the world in August 2020.

"Having a baby in a pandemic has definitely been a strange experience, however she is growing up so fast and at 10 months old is changing every day. I returned to work in May and I have enjoyed being able to have a warm cup of tea and some lunch! Willow is enjoying childcare and making a lot of new friends."

Introducing our new recruits!

We're delighted to welcome three new members to the Eastwood Financial Services family in this issue – Anthony Kelly-Rimmer, Paul Atkinson and Bradley Booth.

Anthony and Bradley both join us as Paraplanners. Anthony said: "Everyone has been very friendly and supportive... they have made me feel very welcome". Bradley agreed saying: "Everyone has been super helpful and polite in welcoming me to the Eastwood team and I can't wait to get properly stuck into everything!"

Meanwhile Paul has joined us as a Financial Adviser and commented: "It feels like I've been here forever (in a good way)! From day one I have been made to feel welcome by everyone at Eastwood Financial. It is great to be part of the team who have offered so much support and help, it has made settling into my new role much easier.

We wish them all the best in their future with EFS!

Giving you financial freedom

Eastwood Financial Services is committed to offering independent, careful and comprehensive financial planning to both businesses and private clients.

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