Edward T James & Company

Issue 02 - June 2009

Welcome to the second issue of the Edward T James & Company Newsletter

AS THE world of financial services continues to evolve, we have gathered together a selection of articles and views that we hope will be of interest and give you an insight to the factors affecting your wealth.

April 1st was an important date for us here at Edward T James – it landmarked our first year as an established professional advisory practice. There have been many challenges for us over this period and it would be true to say that we have enjoyed every minute of it!

By far the most satisfying element for us has been introducing you, our established and highly valued clients, to our vision of how we believe professional advice should be delivered.

We thank you for your trust in us, and for all the feedback we have received endorsing our approach and appreciating our unique personal service.

We hope that you enjoy our latest newsletter – if you have any comments or questions we would of course welcome your contact at any time and look forward to hearing from you.

Chris Polawski and Simon Bullivent

From Inflation to Deflation

A Case of Frying Pans and Fires?

JUST a few months ago, inflation was the spectre that stalked us all. By September, inflation had soared to 5.2%, fuelled by high prices for food and energy. However, following sharp falls in commodity prices and declining demand for goods and services, inflation no longer appears to be a problem and deflation is the new threat.

Deflation is defined as a persistent and sustained decline in prices. A sustained deflationary spiral can help to exacerbate recession as, although some people might welcome an environment of falling prices – particularly after a period of high inflation – a sustained period of deflation could have very negative consequences for the struggling UK economy.

In a deflationary environment, consumers will delay making purchases, believing that prices for goods and services will continue to fall. This delay makes it harder for companies to sell their products, forcing them to slash prices and leading to lower profits, declining wages and job losses. In turn, the reduction in disposable income further impairs demand for goods and services, creating a sustained and damaging spiral.

The Bank of England (BoE) and Chancellor of the Exchequer have taken aggressive actions to try and avert a prolonged period of deflation by cutting rates and introducing a programme of fiscal stimulus. However, even with billions spent and the recent slashing of rates, a risk of below-target inflation still threatens and no one knows how long it will last.

Contact Us
Edward T James & Company, 4c Falmouth Business Park, Bickland Water Road, Falmouth , Cornwall , TR11 4SZ
01326 218261 | enquiries@edwardtjames.co.uk | www.edwardtjames.co.uk

2009 Budget Overview

A Mixed Bag in Difficult Times

AS THE Treasury struggles to cope with the cost of the recent bank bailouts, the rising cost of social security and falling tax revenue, public borrowing is set to soar to record levels. In an attempt to help the UK balance its books, Chancellor of the Exchequer Alistair Darling intends to cut growth in spending on public services by almost half from 2011 and, in a surprising move, he announced that those earning more than £150,000 per year will be taxed at a new high rate of 50% and have tax relief on pension contributions reduced from April 2010.

ISA limits will be raised from £7,200 to £10,200, which is welcome news for those who have seen savings income slashed but savers will not be able to benefit immediately.

The increased ISA limits will only apply to those aged over-50 this year. However, these savers will not be able to take advantage of the new limits until October to give providers the chance to adjust their systems. Other savers will have to wait until next year to take advantage of the new limits.

Fuel duty will rise by 2p per litre in September, while duty on alcohol and tobacco rose by 2%. Darling announced £2 billion-worth of help for the unemployed, and measures intended to boost the housing market and the motor industry. The Budget included some help for businesses, although the Confederation of British Industry criticised the Budget, commenting that it did not set out a "credible and rigorous path for restoring the public finances to health."

Pensioners will see the basic state pension increase by at least 2.5%, regardless of inflation, and current winter fuel allowances will be maintained for another year despite the recent fall in energy prices. The limit on savings that pensioners can possess before their Pension Credits are reduced will rise to £10,000 in order to help those negatively affected by low interest rates.

Darling expects Britain's economy to shrink by 3.5% during 2009, and return to growth the following year. However, the International Monetary Fund expects the UK to contract by a rather more drastic 4.1% in 2009, and does not expect Britain to return to growth during 2010.

There is Light at the End of the Tunnel

A Personal View by Simon Bullivent

ONE of the questions we are frequently asked is 'how can we be so confident that after such a deep financial crisis there will be a recovery?' Following such rapid declines in investment values and adverse publicity this can often seem like a leap of faith to a nervous investor.

The first point is to learn from history. Fluctuations in stockmarkets related to crises and events can be charted back for more than 100 years. On every occasion, whether it was the 1929 crash, the 2nd World War, Black Wednesday or the "technology bubble" of 2001 there has been the same result: markets have not only recovered but significant growth has followed.

Secondly, it can be useful to put things into perspective. This time round the falls in value are no greater than experienced in other crises of other years. What was different last year was the speed at which it happened. But what has also been different is the response by governments globally, which can only be positive. Never before has such a collective responsibility been taken to ease the pain and create the environment for recovery.

This leads to another positive element in my view. The jolt to the financial system has created an unstoppable momentum from global authorities to reform and properly regulate and control the various components in a resolute and coordinated manner. Doubtless perfection will not be achieved, but we must be looking at a vast improvement to the apparent laissez-faire and incompetent self regulation demonstrated by the financial institutions to date.

Finally, I would say look to the Emerging Markets to lead us back into positive territory. The significant players are Brazil, Russia, India and China (abbreviated to BRIC for financial people) where the drive for wealth is fuelled by the desire of literally billions of people to improve their lives. The proposed spending on infrastructure is colossal, and along the way these countries are massively expanding there own markets for demand – for example, the middle classes in India are now estimated to number over 300 million. This all has a positive knock on effect for the western economies, as demand for our products, services and expertise in these countries increases.

Many commentators now agree that markets are becoming more stable and we have reached the bottom of falling stockmarkets (although of course there is never a guarantee of this!). We at Edward T James & Company have tentatively noted that there are now a number of investment funds showing growth when projected back over 5 years. There is a phrase in financial planning that I consider holds as true today as when first spoken over 100 years ago: "successful investment is not about timing, it is about time."

Multi-Manager

Providing Diversity in your Investments

THERE are now over 2,000 UK domiciled funds available to investors, plus a whole array of offshore funds. Very few fund managers deliver good returns all the time and even the best fund managers will go through bad patches. Using a good multi-manager could therefore help give you some reassurance that your portfolio of is being managed by an investment expert all the time. Multi-managers are experts in selecting only the best funds and they offer packages of these to investors, based on their proprietary research.

Multi-managers meet fund managers individually and quiz them on their holdings and potential for long-term performance. They can also discover hidden gems that may not be available to private investors due to being offshore or having high minimum investment levels. Multi-managers will also be experts in building a portfolio as they will know how to blend certain funds or managers together to minimise risk and maximise returns.

The two main types of multi-manager are fund of funds and manager of managers. Fund of funds managers build a portfolio of funds based on their research techniques and will then buy or sell funds as market conditions change. Typically, these funds might be split into cautious, balanced or aggressive, each set up with different weightings in different asset classes, designed to suit different types of investor.

Manager of managers funds invest allocations of a total portfolio with different pre-selected managers, based on who offers the most suitable expertise. They give that manager a pot of money to manage and then set specific guidelines as to how that money should be run. This money is run separately to any other portfolios and is run for the manager of manager fund exclusively.

Multi-manager products can be more expensive than single manager funds because there are two layers of charging – one to the multi-manager expert and the other to the underlying fund or manager. However, they can often negotiate discounts as they effectively buy in bulk and are a great one-stop shop solution, either as a 'core' investment to form the bedrock of your wider portfolio or as a first step into the world of market investment.

Quantative Easing

The Financial Term for "Printing Money"

THE BANK of England (BoE) made history in March 2009 with the news that it was to begin a radical programme of quantitative easing. Quantitative easing helps to increase or reduce the supply of money held in commercial banks' reserve accounts at the central bank. The BoE will buy £75 billion-worth of securities from commercial banks, and will pay for them by adding money electronically to the banks' reserve accounts. In May this figure has increased by a further £50 billion.

Although quantitative easing has been described as "printing money", the BoE does not put new banknotes into circulation; the process is purely electronic, although it does result in the creation of new money. Importantly, the BoE is not giving money away; it is buying assets from the banks, and it will sell these assets at a later date, reversing the effects of quantitative easing. However, it is vital that the BoE gets the timing right and reverses the policy before inflation is driven too high.

The BoE hopes that banks will weary of squirreling away their cash for a minimal return and decide to lend out the money at a more profitable rate, making it easier for companies and individuals to get mortgages and loans and helping to revive spending. A lack of credit is one of the most significant problems confronting the UK economy, so action that increases the supply of money and the availability of credit is welcome. However, whether the commercial banks choose to increase their lending activity or hoard the additional capital remains to be seen.

Inheritance Tax

The Final Attack on your Wealth

DESPITE the threshold rising to £650,000 for married couples and civil partners (£325,000 for individuals), the boost in house prices over recent years means inheritance tax (IHT) is still a concern for many homeowners. It is therefore sensible to consider the potential liability you may be leaving behind.

Before you look to offset it, however, it is important to sort out what will accumulate as a potential liability. For most the key contributor to their estate will be the value of their home but, even if this lies below the threshold, there are other elements that can push an estate over the limit. For example, while people typically talk of the benefits of ISA investing, although it shelters investors from capital gains and income tax, it does not shelter the value from IHT. Another example is that any property held abroad also goes towards the value of an estate. Both are therefore susceptible to inheritance tax.

The problem with this tax is not just the fact it has to be paid, but also that it has to be paid quickly – generally within 6 months. Passing on your home or other heirlooms intact could therefore be compromised as, without planning, some may need to be sold to meet the bill.

However, there are things you can do, particularly if your liability is relatively small. Few people realise that they have an annual exempted amount that they can gift to someone. At £3,000 per year this could go some way to reducing the overall estate. Gifts for weddings, from parents, grandparents and even friends, are also exempt (subject to varying maximum amounts) and there are other useful tools such as loan trusts and discounted gift schemes.

The new exemption on business assets is also an interesting development. As long as the assets are held for more than two years, they should be seen as IHT-free and this includes shares in the smaller companies stock market, AIM (although, do note that these stocks can carry higher risk and should not be held purely for tax reasons). Added to this, there are partially-exempt trust structures.

As the Government looks to close any potential tax loopholes it is worth getting advice on what can and cannot be done to ease potential IHT burdens.

Alternative Investments

Can Provide Opportunity and Spread Risk

ALTERNATIVE investments have become much more popular among investors in recent years and many mainstream asset managers now routinely offer this type of product. Such alternatives might include hedge funds, property, private equity vehicles, commodities or even antiques, fine wine and classic cars. Each has its own performance characteristics and each can provide different benefits when combined with a more mainstream portfolio.

The main reason for including alternative investments in your portfolio is that these performance characteristics are likely to be different to the mainstream asset classes of bonds, equities and cash.

Consequently, although some alternatives might be considered higher-risk when judged alone, their inclusion in a wider portfolio can actually help to reduce risk by diversifying the portfolio overall. As they tend not to move in line with traditional bond and equity markets, they can be used to defend a portfolio at times of bond or equity market volatility.

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Edward T James & Company is the trading name of Edward T James & Company Limited registered in England No. 6475673.
Registered Office: 1 Water-Ma-Trout, Helston, TR13 0LW.
Directors: Christopher Edward Polawski and Simon James Bullivent.