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# Personal Wealth Outlook

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## Smart growth—How we are expanding

Growth is important to any organism and our business is no different. Standing still can seem an attractive option when you are busy, but doing so can mean that you take your eye 'off the ball' of clients' requirements. That is why we have recently expanded by taking over an existing successful Ascot-based firm, the Scrivener-Evans partnership, which focuses on private clients. "This will ensure that we can not only continue to provide a high standard of service to our existing clients," comments Sanjay Shah, partner, "but also move forward to expand the level of back-up available to clients through the introduction of additional skills."

Mike Scrivener has joined Smart Wealth Management LLP as Director of Private Clients and will be responsible for developing the partnership's offerings in this area. "I am delighted to have the opportunity to join a vibrant and expanding business at this exciting time," commented Mike. "With so much market turbulence—and so many opportunities for investors—we can expect to see considerable change over the next year or so as we are determined that our clients will benefit to the full."

## Things could be worse—and could get much better soon

According to American investment guru Warren Buffett, now may be the time to invest in equity markets; strange as it might seem. One of the wealthiest investors in the world, he has made his money—and, to be fair, lost some too—by not following the investment 'herd' but being prepared to be different.

If this sounds counter-intuitive, it is worth considering that markets are currently undervalued in historic terms, so that there is scope for a significant recovery. What is not clear is when this will take place, or how long it will last. Nor are there any guarantees; that is not how investment markets work.

But every fall in market values to date has been followed by an upsurge in prices.

If there was a simple recipe for investment success, everyone would be rich! In fact, any general comments always need to be viewed with a discerning eye, selecting only those indicators which appear to accord with the individual's attitudes towards risk and reward. According to Buffett, the key to success is being prepared to be different from everyone else. Writing in the New York Times on 16th October 2008, he wrote: "Be fearful when others are greedy, and be greedy when others are fearful." What he really means is that you should buy at the bottom of the market and sell at the top. By following other investors too closely, you can frequently end up doing the exact reverse. That is why it is so important to take professional independent financial advice before making any investment decision; and why we are here to help you.

## Undervalued markets

Despite the best efforts of the press to scare us all with tales of doom and gloom, not all the news is bad if you take a long-term view. FTSE100, which covers the largest companies in the UK, has been running in its current form for just under 25 years now. Starting in April 1984 at a base of 1,000, it ended December 2008 at 4,434, well down from its high points of 6,930 at the very end of 1999.

At that time many commentators were concerned that most world stockmarkets were overvalued and that a correction was inevitable. Which, of course, is what happened during the early years of the century; with the FTSE100 falling to 3,287 in mid-March 2003. It then rose back again reaching 6,732 in mid-June 2007 before falling back.

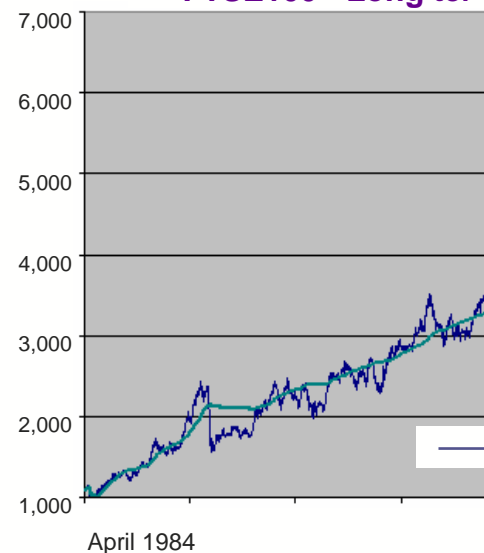
### Why the history?

First we wanted to demonstrate that markets are volatile and should be viewed only over the longer term; they are influenced by external events such as the credit crunch just as much as by the inherent stability of companies that we all invest in and their ability to continue paying dividends.

Secondly, we wanted to draw attention to the long-term trends inherent in the figures. By creating an 'average' of the FTSE100's daily closing prices over the entire period, we can add a 'trend' line for the index.

What is really interesting is that the index is currently some 30% below its long term trend line. This could, of course, simply reflect that the market was, indeed, overvalued and therefore represents a correction that will remain in place for some time. But this

FTSE100 - Long term



would assume that markets act in isolation. In fact, they are influenced not just by economic factors but also the pressure of money available for investment.

For the past year, money has become relatively scarce as people sell assets on a falling market—and feel less well off, because of falling house prices. This has exacerbated the problem of falling share values as fewer investors chase an increasing number of available shares. But this will eventually be offset by the pent-up demand amongst individual investors, who need to make provision for their retirement, and institutional investors, seeking a home for their funds.

### **The future is bright**

The result of this is that we can expect share values to bounce back at least in the direction of their long-term trend, as soon as confidence starts to return to the market. The election of Barack Obama could also be an engine of growth.

It is important to remember that the actual components of any index such as the FTSE100—the companies which are used to calculate its value—are not constant. Mergers, acquisitions, new entrants and the decline of some old companies combine to ensure that the index constantly reflects the fortunes of the largest companies in the UK by market value.

### **Uncertainty will continue for some time**

Of course, markets could eventually fall so far that the underlying assets become worthless. This 'Armageddon scenario' in which bartering returns and we swap our labour for goods/services is simply not going to happen. The doom-mongers who speak of shares and bonds becoming 'worthless' are wrong. Some shares *may* lose their value—but only if the companies concerned fail with greater liabilities than assets. Similarly, certain corporate bonds and even some sovereign debt will become worthless paper, but only if issuers default on their obligations.

By far the majority of listed companies will remain in business—and most will continue generating profits, throughout a global recession. The vast majority will continue to meet their debt obligations too—though some will fail.

Bonds have a value determined by the rate of interest it pays, the security of that interest and the security of eventual repayment. Shares too have a value determined by underlying corporate asset base, prospective profits and potential growth (or reduction) in future profits. Markets merely provide a pricing mechanism; arguably, global financial markets are increasingly distorted and inefficient in this regard. Presently they are driven by fear of further falls, which drives investors to sell stock. Panic has replaced sober assessment of corporate balance sheets and of realistic lower earnings prospects.

In the bond markets, stock is being dumped – not because it is fundamentally unattractive, but because many bondholders (e.g. hedge funds) borrowed to buy it and are now forced sellers, as their lenders demand repayment and they fail to secure alternative funding. The bond market is therefore subject to severe distortion.

Investment grade bond yields are already very attractive and will become more so, as interest rates reduce dramatically and inflation falls next year. In the meantime, holders of bond funds are uncomfortable – with their funds (traditionally a safer asset class) falling in value to an extent not typical of this type of asset. We expect a strong bond rally – with a surge more usual of equities but the big question is when. For those buying now, yields are highly attractive.

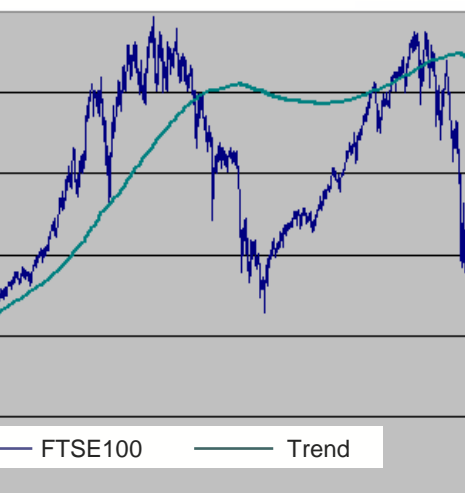
Dividends from equities will become more attractive to investors too, as deposits produce a lower return and bond yields fall, as prices rise. As the equity markets fall, perceived risk bottoms out, whilst investors are forced to seek better returns when deposit rates fall significantly. Those accustomed to 4-5% pa on deposit will have to invest elsewhere as interest rates fall – or accept a considerably reduced return. Many will have no choice but to return to the equity and bond markets.

Financial markets will only properly reappraise the value of equities and bonds when credit conditions ease, interest rates fall further and the likely depth of the global recession becomes clear. Panic and volatility will prevail until then, but the tenacious investor will eventually be rewarded handsomely. In the meantime, the first building block of recovery – stability in the global banking system – seems to be in place.

You should consult your usual **Smart Wealth Management** LLP Financial Planner before making any decision relating to your personal finances. The value of investments is not guaranteed; you may get back less than you put in.



### **FTSE100 trend to end 2008**



December 2008



## End of tax year tax planning—don't miss the boat

The start of a new year brings with it—thanks to our rather arcane fiscal arrangements—the approaching end of the tax year on 5th April.

If this sounds a long way off, you must still be young enough that the days do not fly by faster than you can turn round; for the rest of us, the deadline is looming.

The main point to consider is that there are some cut-offs on the last day of the financial year that are difficult, some impossible, to get round if you miss them.

Most important of these are as follows.

- **Pension contributions**—thanks to a change in the rules a few years ago, pension contributions now have to be made before the end of the tax year, there is no longer a provision to carry them back into a previous year, neither can 'unused' tax relief be carried forwards into the next tax year. This means that you can make a contribution of up to your entire earnings (subject to a maximum of £235,000, this year) effectively up to the close of business on Friday 3rd April 2009, or the year's allowance is lost and you will have to apply any contributions you wish to make towards next year's limit, which is up to £245,000. The 2008/9 allowance is lost forever.

An employer can top up from annual earnings to the annual allowance, but the same deadline applies.

- **ISAs**—Each individual can invest up to £7,200 a year into an Individual Savings Account, of which up to half can be in cash. Rebalancing previous years' contributions from cash to equities does not affect the annual limit but, as with pensions, contributions that miss the end of tax year cut off are lost for good and have to be applied to the next year.

Pensions and ISAs protect investments against UK income and capital gains

tax (although there is no option to recover the 10% withholding tax on dividends from UK companies) and, in the case of pensions, contributions receive tax relief at the individual's highest marginal rate.

- **Venture Capital Trusts (VCTs)**—these work slightly differently and are designed to encourage individuals to invest indirectly in a range of small higher-risk trading companies whose shares and securities are not listed on a recognised stock exchange.

They offer income tax relief on investments of up to £200,000 during any tax year at 30%, even for a standard rate taxpayer, although you cannot receive more relief than the amount of tax you are liable to pay—and any excess cannot be carried across to offset tax in any other year. In addition to this relief, dividends received are free of UK tax, as are capital gains, after shares have been held for at least two years. It is also possible to use VCTs to 'roll over' capital gains tax liabilities.

The availability or otherwise of tax reliefs are not, in themselves, an adequate reason for making investments. After all, there is no point in avoiding tax on gains or income if there isn't any.

As a starting point, you should consider the suitability of the investment you are proposing to make as an investment, taking due account of the asset allocation strategy that best suits your investment goals and attitude towards risk.

Only then should you go on to consider the tax implications of the investment you propose making.

It is important always to seek independent financial advice before making any decision regarding your finances. For further information, please contact your usual **Smart Wealth Management LLP** Financial Planner.



## Pension statements—not pretty reading, perhaps ...

About now, many people receive a statement of benefits relating to their pension benefits.

Members of defined benefit (final salary) schemes—most of whom are in taxpayer-funded government schemes—have nothing to worry about; for the rest of us, there is an ‘opportunity’.

If your pensions benefit statement shows that, despite you (and possibly your employer) having invested good money this year, your scheme is actually worth less than last year you are likely to be disappointed. But in fact, things are not necessarily as bad as you may think, unless you are just about to retire. And even then, you have some options that may make matters easier for you.

### Plenty of time to go?

If you have five or more years to go to your chosen retirement date, there is time for your pension fund to recover from the recent downturn in equity markets. Most markets are currently significantly below their long term trend values (see ‘Undervalued markets’ opposite) so there is every possibility that fund values will recover as the market goes up.

It is also worth considering that fixed contributions made during recent months will have purchased many more shares (or fund units) than a year ago. The effect of so-called ‘pound cost averaging’ is actually beneficial when equity values start to rise again, because you will have more shares for your investment, than had values simply continued rising steadily during the intervening period.

### An extra opportunity

But low market values also offer a special opportunity for those in a position to make an investment now. Imagine, for a moment, that you earn £50,000 a year and have just inherited a similar amount. If you normally invest 10% of

your income into your pension and your employer puts in 5%, you will be putting aside £7,500 a year. But new rules introduced in 2006 now mean that you can invest up to your entire earnings into a pension, plus anything your employer puts in, provided that together you do not exceed the annual allowance (which is £235,000 for 2008/9 and is set to rise in future years).

This means that you could now contribute a further £45,000 into your pension fund (less 20% tax relief, so you actually only have to put in £36,000 to get the same investment value and, as a higher rate taxpayer, you will get back more relief, up to 40% of the contribution, although you cannot get back more in relief than you would have paid in tax! With investment markets at long term lows, now could be just the time to take advantage.

### Retiring soon?

If you are close to retirement and have seen your fund value drop significantly, there is one thing you might like to consider. Rather than using your fund now to purchase an annuity—effectively locking in the losses for ever—you might like to consider taking your 25% tax free cash now and using an “unsecured pension” (what was called drawdown) to leave the balance of your fund invested in equities, in the hope that values will recover and you can buy an annuity later.

Of course there are costs associated with this approach and, as ever, you should take individual professional advice before making any decision relating to your personal finances. The value of investments can go down as well as up; you may get back less than you put in.

You should consult your usual **Smart Wealth Management** LLP Financial Planner before making any decision relating to your personal finances. The value of investments is not guaranteed; you may get back less than you put in.





## Property as an investment—do falling prices matter?

With house prices having plummeted recently—and commercial property being no better—what are the options for property investment?

As with equity markets, low prices could well be creating buying opportunities for those who are able to arrange suitable finance. Within the housing market there could be opportunities for those wishing to move into the buy-to-let market, but mortgages are difficult to come by at the moment and professional advice is essential.

However, that said, it is possible that as more and more people find it difficult to meet their mortgages, increasing numbers of properties could come on the market, further depressing prices, but also increasing the potential rental market.

## Commercial property a better option?

With commercial property, which is particularly attractive for self invested pensions, the issues are slightly different, in that lower prices could make it increasingly attractive for firms to consider purchasing their business premises.

Although some finance may be required to achieve this, it is also generally possible to use existing pension funds to provide much of the purchase price.

Even if this is not currently held within a self invested personal pension or small self administered scheme, but rather within an insurance company plan, it should be possible to arrange a transfer of funds to facilitate the purchase.

It is important, however, to consider the impact of any penalties that might apply.

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## Boiler rooms—a hot place to avoid

So called 'boiler room' fraud, is a sophisticated scam that aims to relieve investors of substantial sums of money. With an economic downturn looming and inflation running at relatively high levels, we can expect an increase in the level of criminal activity, as criminals seek new ways of generating an income. Some threats to personal finances do not even need you to be taken in by a trick; instead they rely on the side effects of 'normal behaviour'.

### Identity theft

One of the greatest threats we face today is identity fraud, which most commonly results from the theft of old credit card, utility bills and other statements. These can be used to establish identity so that criminals can set up bank and credit card accounts in your name—and run up large debts, ostensibly as you, which can damage your credit rating. You may have difficulty in proving that the debts are not, in reality, yours. Destroying old documents that identify you is essential.

### Phishing

Phishing is where an e-mail ostensibly from your own bank or someone respected like Google or e-bay asks you to 're-register' your details as they have had a computer failure. Entering your details on the fake website gives the criminals access to your account on the real one; so they can empty your account or incur liabilities for their purchases.

### Computer fraud

A more recent area that needs looking at is that if you use a wireless connection to the broadband, you must use password protection. If you do not, anyone can link in to your home network and not only 'steal' the internet access you are paying for, but also to look at your files, banking details and other information, in order to defraud you.



## Is your protection up to scratch?—checking your cover

Nobody expects 2009 to be an easy year, what with the downturn biting and the prospect of poor investment returns for some time to come. The New Year is therefore a good time to see whether your family protection remains 'fit for purpose'—and whether you can make any cost savings.

When things get tough, there can be a temptation to cut out what are seen as unnecessary costs. This makes sense, of course, provided you do not throw out the baby with the bathwater—in this case, almost literally.

Ensuring that your family is fully protected should anything happen to you is arguably more important during a recession than at any other time, because it is less easy for one parent to go out and find a job to replace the income previously provided by a partner who has died or become long-term incapacitated. (Or, indeed, if they have been made redundant—the new scheme announced by the Prime Minister on the day of the Opening of Parliament in December only relates to mortgages and is limited to a partial guarantee, so the need for insurance could well remain.)

During the first few weeks of the year, while bills are starting to come in and things are otherwise rather quiet, it can be a good idea to take stock of your financial position and consider just what sorts of cover—and how much—you actually need.

For most families, all earners should be insured so that should they die or become ill, there is sufficient income to replace the money they were earning in order to provide enough for the family to live on as well as to cover any mortgage and other repayments.

While no two families will be the same, it is a good idea at least to ensure that all outstanding loans can be cleared by a lump sum insurance and then enough on top to provide for immediate needs, while the family gets back on its feet.



Bearing in mind that the loss of a family member is a stressful time, it should not be assumed that a surviving parent will be able to go back to full time work quickly; not least because of the need to provide support to other family members. For the longer term, earning capacity may remain constrained, so a regular income to supplement wages could be a good idea.

In the case of severe illness, an ongoing income is essential if the family is to continue enjoying an acceptable standard of living.

It should not be forgotten, however, that non-earning partners contribute to the family by undertaking functions that might otherwise have to be paid for, such as cooking, cleaning, care of children and the elderly and so on. As a result, even those who are not 'economically active' should be covered by life and health insurance, to ensure continued functioning of the family, should the worst happen.

### Cost savings

Most insurances become more expensive as you get older, so suggesting that premium savings might be available could sound counter-intuitive. However, it is also true that life expectancy is improving – and with it the nation's health. So it is quite possible that premiums now could be lower than a few years ago, even though you are older.

Finding out whether you could save money while possibly getting more cover is a simple matter of seeking professional financial advice, which is always essential before making any decision relating to your personal finances. It also gives your independent financial adviser the opportunity to establish whether there are any gaps in your protection that can easily be plugged.

You should consult your usual **Smart Wealth Management** LLP Financial Planner before making any decision relating to your personal finances.



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