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Money++

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Cashing in on savings?

The era of near zero interest rates is ending, but are your savings benefiting?

The Bank of England raised its base rate again in June, pushing the figure up to its highest level in 13 years at 1.25%.

The Bank's ratcheting up of interest rates has started to permeate through to the interest paid on savings, although it has often been loan rates which have increased earlier and faster. Unfortunately, you cannot assume that your existing savings accounts have benefitted from the 1.15% rise in the base rate since last December. The banks now have a rare opportunity to expand their margins by widening the gap between deposit and loan rates.

This strategy can be seen most clearly when it comes to accounts closed to new savers. For instance, the rate on Halifax's 60 Days Gold account remains at the 0.01% level to which it fell in July 2020. Switch the money across to a Halifax Everyday Saver account and the interest rate is 0.25% (as of 14 June 2022), with instant access.

At a time of economic uncertainty, when you may wish to build up your cash reserves, you need to look beyond the familiar brand names to find a return that beats the Bank of England base rate. Currently the best instant access rates are around 1.55%.

Contrary to what you might expect, cash ISA rates may be lower than non-ISA rates. National Savings & Investments provides a good example: its Direct ISA pays 0.15% less than its Direct Saver account. While an ISA is UK tax-exempt, in practice the personal savings allowance means you can earn £500 interest tax-free if you are a higher rate taxpayer (£1,000 if your top rate of tax is less).

✢ The Financial Conduct Authority does not regulate tax advice or National Savings & Investments.

Tax treatment varies according to individual circumstances and is subject to change.

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Could you join the one in five?

If you are not a higher rate taxpayer now, you may be soon.

The combination of high inflation and frozen tax thresholds is a toxic mix for taxpayers. Figures from HMRC and the Office for Budget Responsibility show that the four-year freeze to the UK-wide higher rate tax threshold will create over two million new higher rate taxpayers by 2025/26. In Scotland, the freeze only applies to savings and dividend income, but the Scottish higher rate threshold for other income (primarily earnings) is lower at £43,662 and the rate 1% higher.

Mitigate the hike

If you are – or will soon be – a higher rate taxpayer, there are plenty of tax planning points you should review with us, including:

- Ensure that you take full advantage of all your tax allowances, such as the dividend allowance and the personal savings allowance.
- Explore the many opportunities presented by independent taxation if you are married or in a civil partnership.
- Maximise ISA investments – the UK tax-freedom of ISAs is more valuable once you pay higher rate tax.
- Review investments – investment returns in the form of capital gains (maximum rate 20% other than for residential property and a £12,300 annual exempt amount) will normally incur much less tax than income.
- Business owners may have scope to change the structure or adjust the way profits are extracted.
- The higher rate of 40% (or 41% in Scotland) income tax also means that you can receive 40%/41% in Scotland on pension contributions. However, beware the pension annual and lifetime allowance tax traps.

✣ Investments do not offer the same level of capital security as deposit accounts.

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The value of your investment and any income from it can go down as well as up and you may not get back the full amount you invested.

Past performance is not a reliable indicator of future performance.

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

For ISAs investors do not pay any personal tax on income or gains.

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Keeping it real on returns

How you think about investment returns may need to change as inflation soars.

If you could choose between a 3% investment return or a 7% investment return, which would you pick? The answer seems obvious, so let's add some context.

Which is better – a 3% investment return when inflation is 2% or a 7% investment return when inflation is 9%? Once you allow for inflation, the 3% investment return is more attractive as it outpaces inflation; the 7% return means lost buying power over time.

Consider the real rate of return

In an inflationary environment you need to think of investment returns in 'real' terms, removing the eroding effect of inflation. So, in the example, the 3% return becomes a real return of 1% (3% – 2%) and the 7% return is actually –2% (7% – 9%). Taking this approach means short-term, deposit-based investments are much less attractive, despite interest rate increases.

The past 13 years of near zero interest rates, combined with low inflation, have encouraged investors to focus on the capital growth element of investment returns, favouring technology-related companies. Inflation and rising interest rates have reduced the appeal of distant profits and the other component of investment return, income, has now become important.

However, inflation is not all bad news for investors. Many companies aim to keep their dividends growing at least in line with inflation over the longer term. Link Group, a leading share registrar which monitors dividend payments, recently said that it expected regular dividend growth of over 15% this year.

If you want to protect your capital from the ravages of inflation, there are plenty of potential options, but none is without risk, so advice is important.

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Are you facing a retirement challenge?

With double digit inflation on the horizon, you may need to reassess your plans.


Credit: RobSimonART/Shutterstock.com

In May, a report from the Bank of England's Monetary Policy Committee bleakly predicted "We expect inflation to rise to around 10% this year". The Bank pins the blame on energy prices, the Ukraine war and supply chain issues. None of these has a clear end date, but the Bank expects inflation to be "close to our 2% target in around two years". Whether or not their forecast proves correct, if you are close to, or about to, retire the immediate outlook is unsettling. So, what should you do?

The starting point is to do nothing until you have sought advice. Some aspects of retirement can be impossible to unscramble once set in motion. Your pension arrangements may state a specific retirement age but you may also still have choices.

Crunch the numbers

Your next step is to work out your likely expenditure and income in retirement. This needs to be a realistic assessment – a recent survey found that two fifths of 2021 retirees were already spending more than they had expected. We can help with the complex calculations using software that can handle assumptions about differing rates of inflation (considering the impending 10%) and investment returns.

Identifying future income and spending patterns is vital in understanding what your options are. Cash flow analysis can show whether the level of investment risk that you are normally comfortable with is compatible with your retirement spending plans.

Bear in mind that at 65, average life expectancy is 20 years for men and 22 years for women. If the calculations suggest that you will outlive your retirement fund – a common concern for recent retirees – then you could consider revising your expenditure plans or accepting that at some point you will need to trade down to a smaller property or look at other options to extract value from your home. At the opposite end of the financing scale, the data might show all your needs can be met with an index-linked annuity, carrying no investment or duration risk. However, sadly that is unlikely as at current RPI-linked annuity rates the standard lifetime allowance of £1,073,100 will provide a monthly income of about £2,850 before tax.

In the worst case, a cashflow analysis may force you to consider deferring or phasing in your retirement. That may seem an unpalatable option, but it is better to be aware of the situation before your earnings have ended. A survey of 2022 retirees found that a fifth were retiring later than they had originally planned, with the main reason for the delay being not having saved enough. An extra period of work – whether full or part time – reduces the pressure on your retirement savings and may allow you to continue your contributions rather than making withdrawals. For advice tailored to your circumstances, please contact us.

✢ The value of pensions and investments and the income they produce can fall as well as rise. You may get back less than you invested.

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Occupational pension schemes are regulated by The Pensions Regulator.

Equity Release will reduce the value of your estate and can affect your eligibility for means tested benefits.

Travel costs checklist

Many Brits will take their first holiday to Europe this summer since Covid and the implementation of Brexit. Be aware of extra costs and additional paperwork requirements.

Do I need a visa?

Holidaymakers currently just need a UK passport, but from the end of 2022 they will need a ETIAS visa waiver. This lasts three years and allows unlimited trips during this period.

Roaming charges

You may have to pay roaming charges to use your phone in Europe. Vodafone, Three, Sky and EE all now impose these charges, which typically amount to £2 a day. Other providers, including Virgin, O2 and BT Mobile currently have no extra fees. Exact charges depend on the contract so check before travelling.

Covid costs?

Most European countries don't require UK travellers to take a lateral flow test now, provided they're fully vaccinated. The website reopen.europa.eu gives details of latest restrictions for each country. It also explains how to download the EU Digital Covid Certificate, proving vaccination status.

Travel and health insurance

Travel insurance is always essential, particularly to cover medical bills. Some policies may offer cover should you need to cancel or delay arrangements due to Covid, but not all. European Health Insurance Cards (EHIC) are still valid, if in date. Once these expire you'll need the new UK Global Health Insurance Card (GHIC). This allows access to state healthcare in Europe at a reduced cost, or sometimes for free.

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What I wish I'd known – lessons from the other side of 50

Many younger people now rely on the bank of Mum and Dad to help get them on the housing ladder. But parents may also have some useful life lessons to impart when it comes to saving towards a more secure financial future.


– Credit: fizkes/Shutterstock.com

Research among the over 50s found that half regretted not starting a pension earlier, while almost two-thirds said they wished they had saved more into their retirement funds.

Those embarking on careers today have the benefit of auto-enrolment pensions, with employer contributions, once they earn more than £10,000. Of the over 50s surveyed, 25% delayed starting a pension until they were in their 30s, often putting mortgage payments and family needs ahead of pension contributions. However, financial experts warn that parents' advice is not always correct when it comes to how much to contribute to a pension plan.

A quarter of those aged over 50 think that putting 5% of earnings into a pension will be enough to fund a decent retirement – the current minimum auto-enrolment contribution. Experts disagree, stating that these minimum levels could leave people with insufficient funds in retirement. The Pension and Lifetime Savings Association believes that people should be savings around 12% of their earnings into a pension if they want a comfortable retirement.

Where possible, younger workers should look to increase pension savings beyond minimum levels, and ensure their pension contributions increase with any salary rise. This should help protect against the same financial regrets when they reach their parents' age.

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The Financial Conduct Authority does not regulate auto enrolment.

Charitable giving – doing it right

The war in Ukraine and cost of living crisis have prompted many people to support charities helping those affected. Various schemes can boost the value of your charitable donations.

Gift aid

Charities can claim back basic rate tax on donations, meaning for every £1 you give the charity gets £1.25. This scheme is for UK taxpayers. Higher rate and additional rate payers can also reclaim the tax paid on donations through self-assessment. This can effectively lower the net income at which their tax is calculated, which can be beneficial for those earning just over £50,000 who pay the High Income Child Benefit Tax Charge.

It isn't just big national charities like DEC, Cancer Research or Trussell Trust that use gift aid. If you make a voluntary donation (of at least 10%) on top of the standard ticket price to many museums and art galleries, then the total value of your purchase can benefit from gift aid. You can also use gift aid when buying an annual membership to these organisations.

Give as you earn

Some companies allow employees to make regular charity donations direct from their gross salary, exempting these donations from tax, although they are subject to national insurance contributions.

Charitable legacies

If you leave a charitable donation or legacy in your will, it won't be included within your estate when calculating inheritance tax (IHT). What's more, if you bequeath at least 10% of your net estate to charity, any IHT due is charged at 36% rather than 40%.

Share gifting

Shares donated to charity are not subject to capital gains tax (CGT). The value will also be deducted from your taxable income, potentially reducing income tax. If a charity can't accept shares directly you can sell them on their behalf, again avoiding CGT, although you will need an instruction from the charity.

✣ The Financial Conduct Authority does not regulate tax, Wills or estate planning advice. Tax treatment varies according to individual circumstances and is subject to change.

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