COVID-19 LESSONS
Financial takeaways from the pandemic experience

ESG INVESTMENTS KEEP GROWING
Legislation catches up with sustainable investment

WHAT IS A MILLION WORTH?
In today's economy, what will £1 million buy?

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SPRING 2021

The bridging Budget

Budget 2021 brought tax freezes and a few surprises

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In this issue...

A year after the Covid-19 pandemic took hold, the careful and gradual moves out of lockdown are hopeful. The impact on the economy, both short and long term, is yet to play out, but there are some planning lessons for individuals that we can take from the last year. Some of these will be affected by the spring Budget. Chancellor Rishi Sunak was under pressure to continue pandemic support measures, but has also set out tax freezes to come which will begin to replenish the country's coffers. Meanwhile, families may well have focused on their financial well-being, including where they choose to invest. With environmental, social and governance (ESG) funds reporting significant increases, we look at how they have become more mainstream in their cross-generational appeal. And for those focusing on retirement, while the state pension increases in line with the triple lock, we look at what £1 million is really worth long term.

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PLANNING

Universal reality check

The challenging reality for many people of having to make ends meet on benefits during the pandemic was underlined by the widespread calls for the government to retain the 'temporary' £20 weekly uplift to universal credit.

It has become clear that the lowest monthly standard allowance of £342.72 for single claimants under 25 provides a minimal amount to live on. A waiting period of up to five weeks before payment starts also doesn't help.

With unemployment continuing to rise and the precarious state of the economy, it is more important than ever to build your own financial safety net. You need to ensure that you can continue to pay your essential bills and maintain your living standards if you were to meet with redundancy as well as illness or accident.

SAVE FOR A RAINY DAY

The Covid-19 crisis has highlighted how quickly 'safe' jobs can disappear with little or no warning when economic conditions change. So, if there is a chance of becoming unemployed, you'll need an emergency 'rainy day' fund to help cover mortgage payments and other bills.

How much you set aside will depend on your individual circumstances, but a good rule of thumb is to have enough savings to cover three months of essential bills. It may not be easy to put this aside all at once but accumulating small amounts regularly can help build a financial buffer.

The best savings account for an emergency fund is one that gives you easy access. Interest rates are low at present, but it can pay to shop around between instant access and ISA accounts.

INSURE YOUR LIFE AND INCOME

Savings can provide a short-term stop gap if your income disappears temporarily, but insurance provides a more effective safety net against the financial consequences of death or serious illness.

Life insurance is the fundamental building block of most families' finances. A lump sum paid on death can help to pay off a mortgage and other debts or be used to set up a fund to provide an income. Life cover is relatively cheap and, given the very minimal benefits that the state provides, protection shouldn't be left to chance.

Likewise, income protection insurance can provide valuable support if you find yourself unable to work because of ill health. With this type of insurance, the typical payout is two-thirds of your income, although there is usually a 'deferral period' of three or six months before benefits are paid. These payments are more generous than statutory sick pay, which is just £95.85 a week for up to 28 weeks.

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PLANNING

What can we learn from the Covid-19 pandemic?

As we pass the various one-year anniversaries around the Covid-19 pandemic, there are some useful lessons to draw for your financial planning.

The past year has been difficult for almost everyone – including the Chancellor. On 11 March 2020, Rishi Sunak delivered his first Budget, less than a month after becoming Chancellor. It included a set of "temporary, timely and targeted" measures to address the impact of the then new coronavirus. On the same day, the World Health Organisation declared Covid-19 to be a pandemic. In the months since, Mr Sunak has regularly returned to the despatch box to announce further support schemes.

If you take a step back, the pandemic experience has offered some important financial lessons.

THE VALUE OF AN UP-TO-DATE WILL

Over half the adult population does not have a will, and Covid-19 had many scrambling to put something in place, or make changes to an existing will that was no longer relevant. This urgency came just as the practical difficulties of will writing reached a peak, when finding solicitors open for business or arranging appropriate witnesses had become a major headache. Then the issue faded from the headlines with the easing of lockdown in the summer and some temporary legislative tweaks, but the importance of having an up-to-date will remains.

STAY CALM

In the second half of February 2020, the world's main investment markets started to react to the potential impact of Covid-19. Then by about a month later, the value of global shares had dropped sharply, with both the UK and US markets falling by about one third between 19 February and 23 March. Also on 23 March Prime Minister Boris Johnson announced the start of the first lockdown, with the immediate closure of some businesses. Any investor who took fright at the Prime Minister's words and sold up hoping to cut their losses would have chosen the worst time to quit the markets.

Investors who did not panic were rewarded with a recovery that saw some markets close 2020 with a value higher than the starting point. That was not true for the UK, where the FTSE 100 declined by 14.3% over the year. However, from its 23 March 2020 low to the end of the year, the FTSE 100 rose by 24.5%.

YOUR RETIREMENT PLANS CAN SHIFT

The pandemic has had a major impact on working patterns, and by early May, nearly nine million jobs were covered by the government's furlough scheme. Research by the Institute for Fiscal Studies revealed how people also revised their retirement plans. One in eight workers aged 54 and over changed their planned retirement age as a result of the pandemic, with most opting to retire later, not earlier. The pandemic has served as a reminder that events, rather than personal choice, can determine a retirement date meaning retirement plans need to stay flexible.

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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.

The Financial Conduct Authority does not regulate will writing and some forms of estate planning.

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TAX

Spring Budget 2021 – the bridging Budget

The first of two Budgets in 2021 signals larger tax bills in future years.

Once upon a time, the concept of 'Budget Purdah' meant that very little of a Budget's contents trickled out before the day. Major leaks would prompt serious investigations and demands for resignations. The latest Budget underlined how that principle has been eroded. Despite extensive coverage ahead of 3 March, some rumours proved true, others didn't materialise and Mr Sunak still had some surprises.

INCOME TAX

The personal allowance will rise to £12,570 and the higher rate threshold will increase to £50,270 for 2021/22. Both will then be frozen for the next four tax years. In Scotland, the higher rate threshold for non-savings, non-dividend income is set to rise to £43,662 in 2021/22.

Many of the important tax thresholds were once again frozen, such as the £50,000 starting point for the High Income Child Benefit Charge and the £100,000 level at which the personal allowance starts to be tapered away.

PENSIONS

The lifetime allowance for pension savings, which started out in 2006 at £1,500,000, was frozen at £1,073,100 and will remain at that level until April 2026. No changes were made to the annual allowance. The possibility that the Chancellor will reduce tax relief on pension contributions in his next Budget, due in the autumn, remains a real one.

CAPITAL GAINS TAX

The capital gains tax (CGT) annual exempt amount was also frozen for five tax years at its 2020/21 level of £12,300. The Chancellor made no mention of the report he commissioned last year from the Office for Tax Simplification (OTS) on the reform of CGT which he received in November.

INHERITANCE TAX

After being frozen since 2009, the inheritance tax (IHT) nil rate band was due to benefit from an indexation uplift in 2021/22. It did not happen, and the nil rate band joined the freeze-until-2026 tax group. Had the band been linked to inflation since 2009, it would be about £90,000 higher from 6 April 2021.

> *The capital gains tax annual exempt amount was frozen for five years at £12,300. The November OTS report on CGT reform was not mentioned.*

The residence nil rate band will also remain at its current level (£175,000) until 2026. As with CGT, Mr Sunak also has a report from the OTS on reform of IHT in his inbox.

CORPORATION TAX

As widely rumoured, the rate of corporation tax will increase. However, the rise will not take effect until April 2023, when the main rate will jump by 6% to 25%. At the same time a new small companies' rate, equal to the current main rate of 19%, will apply to companies with profits of up to £50,000. A marginal taper will apply to companies with profits between £50,000 and £250,000. The changes will reduce the relative tax efficiency of operating a business via a company rather than as a sole trader.

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The freezing of so many tax thresholds until 2026 counts as a set of stealth tax increases. It will mean that over time, inflation will drag a growing number of people across tax thresholds, triggering new or higher tax liabilities.

If you need any guidance on how the changes (and many non-changes) announced in the March 2021 Budget could affect you, or actions to consider before its autumn sequel, please get in touch.

✣ *The value of tax reliefs and tax treatment depends on your individual circumstances. Tax laws can change. The Financial Conduct Authority does not regulate tax advice.*

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TAX

Going electric: the changing face of company cars

The UK's best-selling car for three months in 2020 did not even have an engine.

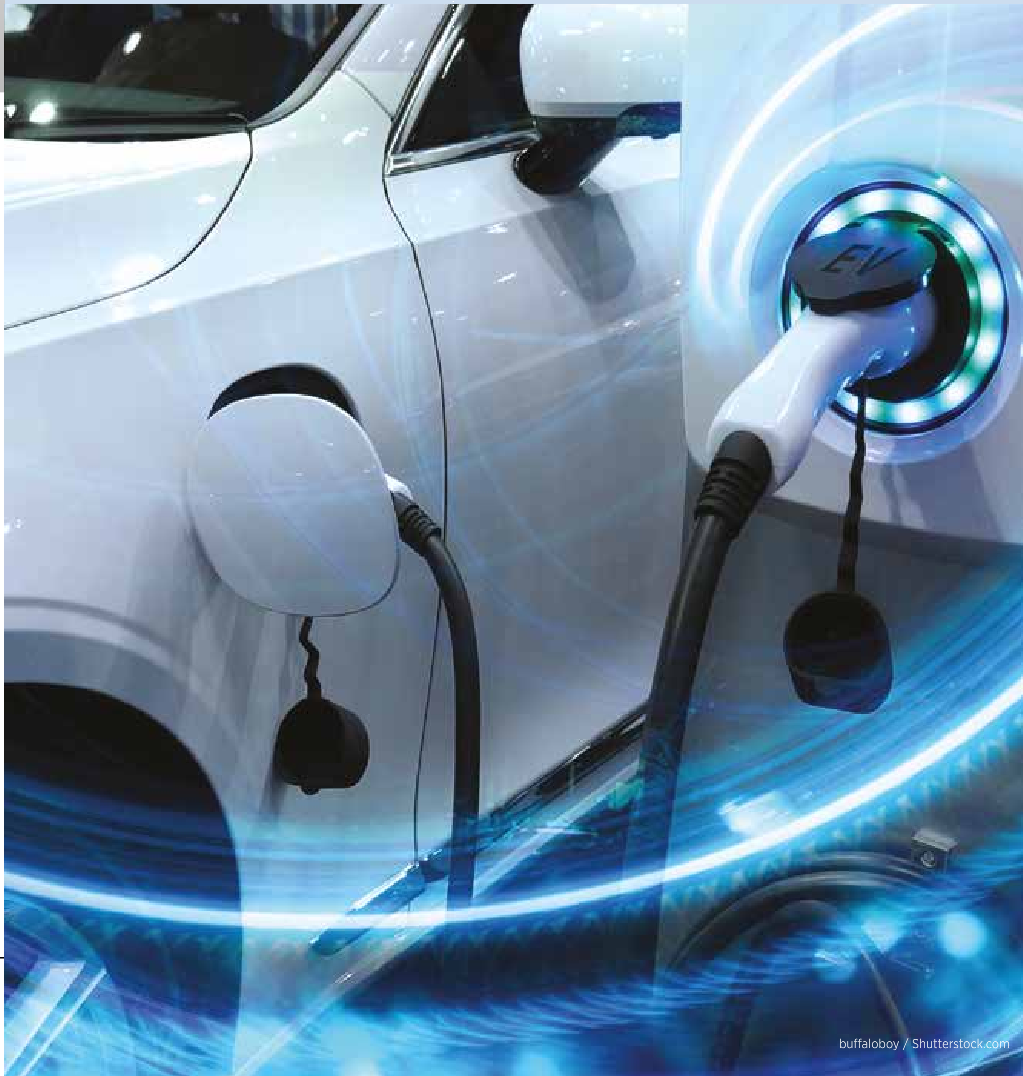
The top-selling car in the UK for the months of April, May and December last year was a Tesla Model 3, a car that currently costs just over £43,000. One major reason for Tesla's popularity is tax. For 2020/21, the employee who chose a zero-emission company car like the electric Tesla paid no company car tax. A BMW 3 series of the same value would have cost a higher rate taxpayer up to £5,200 in tax.

The company car scales have been revised for the tax year 2021/22, but the Tesla is still only taxable on 1% of its value – meaning a bill of about £175 for a higher rate taxpayer. The tax on the BMW is increasing by the same amount.

The tax benefits of going electric extend to fuelling the car, too. There is no tax to pay for electric car charging at the workplace. If the employer fuelled the BMW 3 series, then in 2020/21 the higher rate taxpayer would have up to an additional £2,940 tax to pay – and would probably have been advised to pay for their own petrol.

If you are due to change your company car soon, be sure to consider the electric option.

✣ *The Financial Conduct Authority does not regulate tax (or motoring) advice, and levels and bases of taxation and tax reliefs are subject to change and their value depends on individual circumstances.*



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INVESTMENT

Intergenerational appeal of ESG investing

Since the outbreak of Covid-19, there has been a renewed interest in more responsible and sustainable investment funds.

One outcome has been a significant increase in the amount flowing into funds that explicitly take account of environmental, social and governance (ESG) criteria, alongside conventional financial metrics.

This growing trend has been on the back of a relatively strong performance from the ESG sector, particularly when compared with more traditional non-ESG funds. ESG funds have generally benefited from having less exposure to fossil fuel companies in the oil, gas and mining sectors — many of which were affected by falling oil prices in the wake of global lockdowns and economic downturns.

This shift of ESG factors into mainstream investing is set to be supported by legislative changes, with government encouraging companies to reduce carbon emissions and invest in cleaner energy to limit the rise in temperature and tackle climate change.

These rules extend into the financial sectors: advisers will soon be required to ask clients about their attitudes towards ESG, when advising on suitable investments.

GENERATIONAL IMPACT

Younger investors are often regarded as the most environmentally aware and those driving demand for 'greener' products. But these changes will mean investors of all ages will be asked to consider how their money is invested, and whether they want to bring ESG factors into the investment mix to a greater extent.

Across families, older investors may want to revisit their portfolios and consider what kind of legacy their investment history may leave the next generations. Grandparents are increasingly asking whether it makes sense to invest successfully for profit if the environment suffers in the long term.

Oil companies, mining giants and airlines, for example, may have delivered good profits for investors in previous decades. The question for maintaining a healthy portfolio, however, is whether their business models will remain as profitable as the world transitions to a low carbon economy, or whether there are more exciting growth opportunities in companies tackling some of the key issues we face, including reducing waste, cutting pollution or delivering renewable energy solutions.

THE GOVERNANCE FACTOR

ESG funds also consider 'social' issues as well as environmental factors. These might include a company's track record on issues such as executive pay, boardroom diversity, tax policies and transparent supply chains.

MORE TRANSPARENCY FOR BUSINESS PRACTICES

Bad business practices, for example revelations of fashion firms sourcing goods from companies using child labour, can affect brand reputation with a knock-on impact for share prices as a result of customer backlash.

The Covid-19 pandemic may have focused attention on these wider definitions of corporate responsibility, with more scrutiny of how businesses look after their employees and the communities they operate in.

It is important to remember ESG funds don't automatically exclude certain sectors or companies, unlike some 'ethical' funds. ESG analysis is designed to identify potential risks and opportunities, although like all investment judgements, these may not always turn out to be correct in retrospect.

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PENSIONS

State pension rise still locked

The main state pensions will have risen faster than inflation by April 2021, but these state benefits are still low compared with even average earnings.

The new state pension (for those who reached state pension age (SPA) after 5 April 2016) will rise to £179.60 a week in April 2021 and the old (basic) state pension (for those who reached SPA earlier) will be £137.60 a week. Both increases are 2.5%, a rate secured by the so-called 'triple lock', which requires these pensions to rise by the greater of:

- the increase in average earnings;
- the rise in prices (as measured by the consumer price index (CPI)); and
- 2.5%.

Other state pensions, such as the state second pension, rise in line with the CPI, meaning a 0.5% increase from April this year.

The 2.5% increase underlines the value of the triple lock, which this year delivers state pension recipients an increase of 2% above inflation. The new state pension and National Living Wage (NLW) both came into effect in April 2016, but 2021 will be the first year that the pension has been the faster growing of the two (by 0.3%), although this does little to narrow the significant gap between them.

Compare the positions of Jack, aged 64 and Jill, aged 66. In 2021/22, Jack works a 35-hour week for the National Living Wage of £311.85. Jill, at the new SPA of 66, will receive the new state pension of £179.60 a week – less than 60% of Jack's earnings. The question is: why has the government set the new state pension so far below the National Living Wage for a full-time worker? And the answer is cost: the government pays the state pension, but it is employers (admittedly including the government) who have to fund the wages.

According to research from the Organisation for Economic Co-operation and Development (OECD), the UK sits at the bottom of the state pension league table for OECD members – although the new state pension is higher than its predecessor. This lowly position explains why the government has placed so much emphasis on automatic enrolment in workplace pensions since 2012. Similarly, it demonstrates the need for additional private pension provision regardless of any increase to the state pension.

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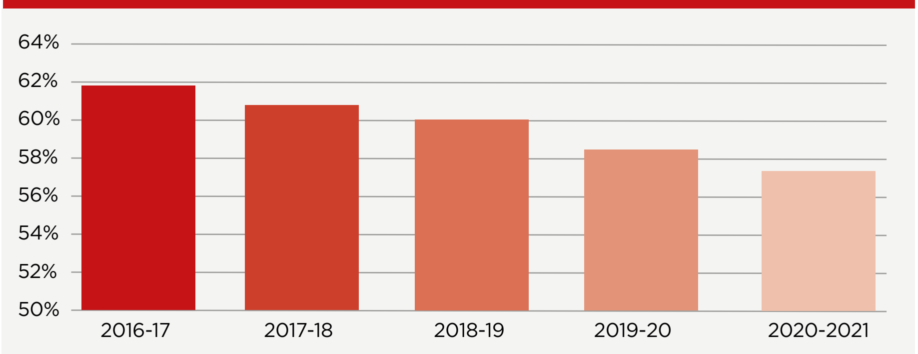
NEW STATE PENSION AS A PROPORTION OF THE FULL-TIME NATIONAL LIVING WAGE



Pension contributions fall in 2020

UK employees contributed less to workplace pensions last year, as the financial effects of the coronavirus pandemic hit.

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> *Recent years have seen significant growth in pension investments: 10 million people had joined a workplace pension through auto-enrolment by 2019.*

Employee contributions into pension plans fell by 11% from April to June 2020 compared with the previous three months, according to Office of National Statistics (ONS) data. Over the same period, which coincides with the first Covid-19 lockdown, employer contributions also fell by 5%. During this time, many people's pension contributions were maintained by the government's furlough scheme.

This temporary fall in overall contribution rates is against a backdrop of significant growth in recent years, with 10 million people having joined a workplace pension through auto-enrolment by 2019.

Membership of pension schemes remains stable, despite these dipping contribution levels, says the ONS, which has not released data on contribution levels for the rest of 2020. We have yet to see the effect of rising unemployment and ongoing economic difficulties on these figures.

Premium Bonds prize rate falls

The prize rate for Premium Bonds has reduced from 1.4% to 1% as savings rates hit a record low. Each £1 bond has just a 34,500-to-1 chance of winning a prize, which may be as low as £25. However, while most bondholders won't win anything, two lucky winners do scoop up £1 million each month.

Rent falls hit buy-to-let

The Covid-19 pandemic brings more bad news for buy-to-let landlords. Rents have fallen in many major cities, because of lower demand for rented accommodation from students, overseas workers, tourists and business travellers. The drop is most pronounced in London, according to Zoopla, but rental prices are also falling in Manchester, Birmingham, Edinburgh, Leeds and Reading.

Regulation of postponed payment services

Financial regulators will now oversee the 'buy now pay later' firms offering interest-free loans to online shoppers. These services allow people to pay for items in instalments and were used by five million people in the last year. There are concerns these interest-free services are an easy way for people to fall into debt, particularly the younger generation. Providers, such as Klarna, will now have to undertake affordability checks.

PLANNING

What is £1 million really worth?

Millions, billions and even trillions now make the headlines, but what do all those zeros really mean, and what will they buy?

You may think you know your billion from your trillion, but it's not quite so simple. Take some quick UK definitions:

- One billion is generally taken to be 1,000 million – 1,000,000,000. Pre-1974, the UK meaning of one billion was one million million.
- One trillion is normally taken to be 1,000 billion – 1,000,000,000,000.

Just as the definitions have changed over time, so has the impact of 'one million' – it is no longer as impressive a figure as it used to be. For example:

- In the UK, just over three million of the population are already millionaires (if their private pension values are included). This fact was highlighted in a report issued at the end of 2020, which examined the possible introduction of a one-off wealth tax to cover the government costs incurred during the pandemic.
- £1 million does not buy that much in the way of income in 2021:
  - At age 65, £1 million will currently fund an inflation proofed pension of around £2,250 a month, or £27,000 a year before tax. Following the recent Budget freeze, the pension standard lifetime allowance remains at only £1,073,100 for the next five years.
  - Placed on deposit at the Bank of England base rate (all of 0.1%), the interest on £1 million will only be £1,000 a year. Even the best instant access account would only pay £5,000 a year.
  - £1 million invested in the UK stock market would generate annual dividend income of £33,500, based on the historic yield on the FTSE All-Share Index.

Billions has replaced millions in the headlines over the past year to report the government's pandemic-driven spending and borrowing. Once all the data is in for 2020/21, the government is expected to have borrowed around £400 billion over the past 12 months. That's £6,000 for every one of the 67 million people in the UK. That will take some repaying: even adding 1p to all income tax rates would only raise slightly under £7 billion a year.

Trillions are rare in a UK context, but currently £2.1 trillion is a key figure: it is roughly both the size of the (shrunken) UK economy and the total (expanded) government debt.

So, what do all the zeros tell you? Firstly, retiring comfortably probably costs much more than you thought. Secondly, with that overall debt figure, you should look to your own financial planning to cut your tax bill, as the government cannot afford to do so.

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