Investment Update

Summer 2017

Brexit: one year on

The controversial Brexit vote took place on 23 June 2016. One year on from the historical referendum, what has changed?

Since last June, the pound has fallen by about 15% against the US dollar and by about 13% against the euro. Sterling's weakness has provided a boost for larger UK companies, whose overseas profits have been enhanced when translated back into sterling, and this has been reflected in their dividend payouts and in the performance of the FTSE 100 Index. The day before the referendum took place, the blue-chip index closed at 6,261. Following the result, the market plunged by almost 9%; one year later, the FTSE 100 Index is over 1,000 points higher.

The pound's weakness has pushed up import prices, stoking inflationary pressures. One year on, the UK's consumer prices index (CPI) has reached its highest level for almost four years during May, rising to 2.9%, but wage growth is not keeping pace with the rising cost of living and this is squeezing UK households.

Political uncertainty has dominated since the vote; David Cameron resigned as Prime Minister after the decision to leave and was replaced by Theresa May. Her Brexit plans were subsequently thrown into disarray by her decision to hold a snap General Election in order to increase her Parliamentary majority – a move that backfired and resulted in a hung Parliament. Looking ahead, the UK is on the back foot as Brexit negotiations begin.

Utilising Business Property Relief

The threshold above which Inheritance tax (IHT) Â is payable has been frozen until 2021.Â Record numbers of families now face the possibility of having to pay IHT.Â

There are products on the market that have been designed to offer investors a faster solution to mitigating IHT which also leaves investors in control of their money.

One such solution is to invest in shares which qualify for Business Property Relief (BPR) as long as they are held for a minimum of 2 years.Â

F H ManningÂ recommend these products throughÂ Â specialist BPR providers and would be happy to discuss this in more detail.

Inflationary pressures bite

The thumbscrews are starting to tighten on UK consumers. Although the cost of living continues to rise, wage growth is not keeping pace with inflation. Inflation's rise has been rapid, stoked by the pound's weakness following the Brexit referendum; in fact, it is less than two years since the UK was in deflationary territory.

The UK's annualised rate of consumer price inflation (CPI) rose to 2.9% in May, compared with April's rate of 2.7%, reaching its highest levels since for almost four years. The Bank of England (BoE) has a rolling target of 2% and, if inflation rises above 3% – one percentage point above target – BoE Governor Mark Carney will have to write an open letter to Chancellor of the Exchequer Philip Hammond setting out the reasons for the move.

Once adjusted for inflation, average weekly earnings fell at an annualised rate of 0.6% in April. The higher cost of living, combined with low wage growth, is likely to hamper consumer demand. UK retail sales fell at an annualised rate of 0.4% in May, according to the British Retail Consortium (BRC), which warned that the slowdown was "indicative of a longer-term trend of a decline in consumer spending power" as inflationary pressures squeeze household budgets.

The UK base rate has remained at an all-time low of 0.25% since August 2016. Looking ahead, recent data are likely to trigger renewed speculation over the likelihood of an increase in interest rates.

Commodities

Commodities are physical assets such as metals, oils, or grains. Commodities offer considerable diversification benefits as their returns tend be lowly correlated to equity and bond markets. Nevertheless, commodities can be risky; prices may fluctuate sharply, influenced by supply and demand and by geopolitical and macroeconomic factors.

Most commodity investors never actually own the physical asset; instead, they invest via a futures contract that requires them to buy or sell a specified amount of the commodity at a future date. However, the easiest way for most private investors to gain exposure to commodities is via a specialist collective investment fund.

US rates rise again

In a move that expressed the US central bank's growing confidence in the economy, the Federal Reserve (Fed) raised its key interest rate by 0.25 percentage points to a range of 1% to 1.25%. This was the Fed's third increase in six months, having already tightened rates in December 2016 and March 2017 and the decision was widely expected. One member of the Federal Open Market Committee (FOMC) voted against the rate rise, compared with eight voting in favour.

The decision took the federal funds rate to its highest level since 2008 when the financial crisis took hold. Back in 2008, the Fed cut its key rate to near-zero levels and embarked on a programme of asset purchases. To date, the Fed has amassed a large portfolio of Treasury bonds and mortgage-backed securities; however, the central bank now intends to start reducing its balance sheet, although its portfolio is likely to remain larger than its pre-crisis level.

The Fed's programme of asset purchases was implemented in a bid to keep US interest rates low and thus encourage business to borrow and invest. In a reversal of that strategy, the Fed's latest move is designed to provide support for interest rates and bring them back to a point that will start to put a brake on demand for loans.

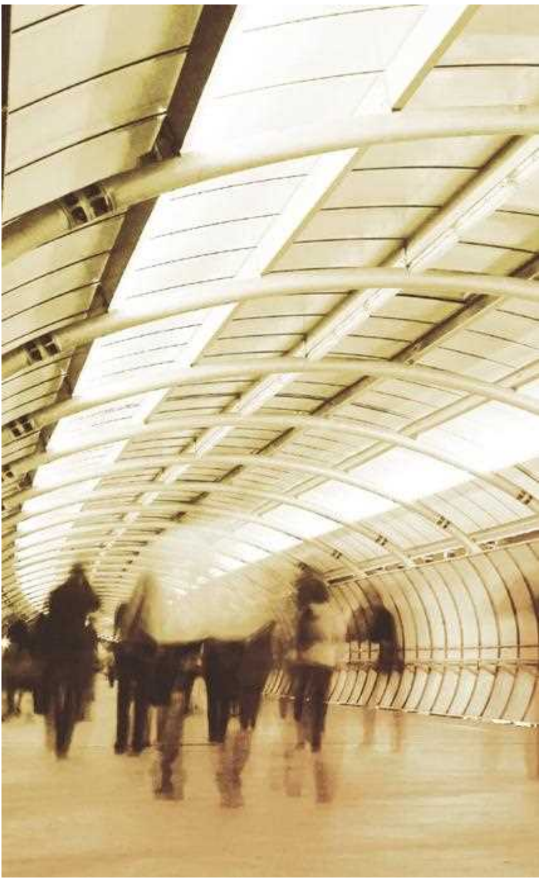
Although there is no definite timetable yet, the Fed is likely to begin this programme of "normalisation" this year, as long as economic growth remains intact. The central bank plans to cut its holdings by a total of US$10 billion per month for three months, after which it will raise the rate of the reductions until they reach US$50 billion per month.

Fed Chair Janet Yellen attributed the FOMC's decision to "the progress the economy has made and is expected to make". The US labour market has continued to strengthen and Fed officials appear to have shrugged off a dip in consumer price inflation: the rate of core consumer price inflation eased to 1.7% in May. The Fed cut its forecast for inflation this year from 1.9% to 1.6%, but still expects CPI to hit its 2% target next year. In the meantime, the FOMC intends to monitor inflation developments "closely" and, looking ahead, the Fed anticipates the "ongoing strength of the economy (to) warrant gradual increases in the Federal Funds rate".

Investment trusts

Investment trusts are collective investment schemes that are listed on the London Stock Exchange (LSE). Unlike "open-ended" investment schemes such as unit trusts and OEICs, investment trusts are "closed-ended": they have a fixed number of shares that can be bought or sold on the stock market.

Whereas the price of units in a unit trust or OEIC is determined by the net asset value (NAV) of the underlying investments, the share price of an investment trust is affected by investor sentiment and by supply and demand, and therefore it will trade at a discount or a premium to its NAV.



Options for care

Demand for long-term care in old age has continued to rise; however, provision remains limited and costs are high. According to Age UK, the number of older people using residential care homes climbed by 21% between 2005 and 2012. The Elderly Accommodation Council (housingcare.org) estimates that care-home fees start at around £400 per week (depending on location and services provided), rising to over £1,000 per week for homes with nursing care.

There are three types of care homes: private care homes, owned by private individuals or companies; voluntary care homes, run by charities or other voluntary groups; and local authority care homes. Other types of care include domiciliary care, which ranges from meals-on-wheels to full nursing care, or sheltered housing, which provides an on-site warden for emergencies, but allows residents to maintain the independence of their own home.

There is very little Government funding for long-term care; only people with assets below £23,250-£25,250 are entitled to financial help (levels differ in England, Scotland and Wales). The unpredictable nature of future care costs, combined with our reluctance to plan ahead for this, mean that pre-funded care plans have become rare. Instead, immediate care plans have become more common. These provide an income in exchange for a lump sum, but can take a considerable chunk out of any investments you have built up, which is another reason to ensure that you make the most of your saving power while you can.

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Planning for inheritance

For the 2017/2018 tax year, the threshold at which you begin to pay inheritance tax (IHT) starts at £325,000 (£650,000 for married couples and civil partners), with an additional “main residence nil-rate band” (MRNRB) of £100,000 per person. However, a little planning can help you to access various annual allowances and exemptions. Regular gifts can be made from income without liability; small gifts can be made annually to children and for weddings and larger sums can become exempt if the donor survives seven years. Alternatively, you can organise funding for beneficiaries to pay the IHT bill via an insurance policy.