

# KENNEDY BLACK

## WEALTH MANAGEMENT

QUARTERLY PRIVATE CLIENT NEWSLETTER

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Welcome to the thirteenth edition of Kennedy Black Wealth Management's Private Client Newsletter.

As we approach the end of the tax year, we point out some key tax issues to deal with in good time. While there are fewer dramatic changes this year, it is important nonetheless. I regularly hear new clients say: "I didn't realise I'd lose the Personal Allowance until it was too late." We explain later on what this means.

We also continue a few recent themes: firstly, about how to improve the chances of financial planning success through a couple of home truths. But we start with a relatively damning indictment of active fund management. Our regular readers should appreciate our passive approach here at Kennedy Black, and the performance figures continue to support that conclusion.

### ACTIVE MANAGERS FALL SHORT YET AGAIN

January saw the strongest start to a year in equity markets since the 1980s.

As our regular readers should know by now, we typically recommend a passive investment approach for a whole host of reasons (cost, control, simplicity etc). However, the most compelling reason in our view, perhaps the most controversial, is that we simply don't believe that even the professionals can consistently get it right.

January brought this home to roost as markets soared. A few stats should help demonstrate this:

The FTSE All Share Total Return Index was up 6.0% on the month. This should be the benchmark for anyone managing a UK equity fund or portfolio of similar risk profile.

The average fund manager (as indicated by the IMA Flexible Investment sector) delivered 5.4%.

The typical financial adviser (as indicated by the Financial Express Adviser Fund Index aggressive index (which consists mainly of actively managed funds) returned 5.4%.

Similarly, the average discretionary fund manager (as indicated by ARC's Private Client Indices equity risk index) returned just 5.7% over the month.

Kennedy Black's passively managed portfolios fared better by comparison, with the adventurous model returning 6.3%.

Admittedly, while the differences aren't huge, this is just one month and the figures are largely reflective of relative performance over the past couple of years.

It is becoming increasingly clear to us that active fund management fails to deliver in its primary aim, namely outperformance.

For a more detailed breakdown of all these statistics, don't hesitate to get in touch. While we don't want to name and shame, we do aim to be as transparent as possible.

### WHO ARE YOU?

To improve your appetite for retirement planning, it turns out it is important to identify with your future self.

A new report from Yale University has suggested that English speakers tend to plan less for their futures than speakers of other languages.

It was discovered, somewhat bizarrely, that languages where there is a weak future tense (such as Mandarin and German) enable speakers to identify better with their future selves, and therefore save and plan more effectively. Those with strong future tenses (such as English and French) are likely to save less for old age, smoke more and get less exercise.

The easy trap to fall into is to treat your future self is another person.

In order to encourage saving for retirement (which is, in effect, a decision to defer spending), one should start to think a bit harder about yourself in a few years time.

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If this feels a little unnatural, try identifying with your past self – say 15-20 years ago. I would anticipate that most people would say they don't feel any different and would ponder as to where all the time has gone.

Now turn that around and think about how you will feel in 15-20 years from now. I suspect not much different either. But you have an opportunity now to ensure you don't feel regret for not having saved enough to support the retirement you want.

### END OF YEAR TAX PLANNING

There are a few points to bear in mind as we approach the end of another tax year. If any apply, don't hesitate to get in touch to discuss things in more detail.

As alluded to in the introduction, the one that consistently catches out the unsuspecting is the earnings trap that appears when annual income exceeds £100,000 in a given tax year. For every £2 you earn over £100,000, you lose £1 of the Personal Allowance (the first £8,105 of earnings which are tax-free). This equates to a marginal tax rate of 60% - until earnings reach £116,200 at which point there is no Personal Allowance left. A one-off pension contribution can therefore attract tax relief at 60%, one the most tax efficient (and least aggressive) forms of saving available.

Child Benefit works in a similar way, scaling back as the highest household income increases from £50,000 to £60,000 pa. Careful pension contributions can attract income tax relief (at 40%) as well as the reinstatement of your Child Benefit.

There are a number of other things to be aware of relating to pensions, particularly if you are a 50% tax-payer and have made or

plan to make sizeable contributions to a pension. With the top rate of income tax reducing to 45% from 6th April, pension contributions will be more tax efficient in 2012/13 than 2013/14.

Similarly, the Annual Allowance (the maximum you can contribute to a pension and still claim tax relief) will be reduced from £50,000 to £40,000 in April 2014. While three unused previous years can be carried over, it is important to note that a pension must be in existence to do so. If you don't have a pension yet, it may be worth opening one before the end of the tax year. If you'd like us to crunch the numbers for you, please get in touch.

As in previous tax years, make sure you take advantage of all the tax allowances and exemptions at your disposal. The annual ISA allowance (or Junior ISA and Child Trust Fund, for children) and the annual CGT exemption are good examples of this. Consider crystallising any unrealised gains in a considered fashion so as not to incur unnecessary Capital Gains Tax (relatively easy on a portfolio of shares and funds; not so easy on an investment property).

While VCTs and EIS investments also carry annual limits, they are much higher (£200,000 and £500,000 respectively) so are less likely to be much of a problem to most investors. However, these investments tend to launch late in the tax year, so do get in touch if you'd be interested to discuss some of the latest opportunities.

There are also Inheritance Tax planning points of which to be aware, such as £3,000 which can be given away in each tax year without attracting IHT. If you didn't use this last year, one year can be carried forward (meaning up to £6,000 could be given away in one go).

Please get in touch if you have any specific end-of-year questions.

### IRRATIONAL BEHAVIOUR #3:

#### *"Over-confidence"*

When a group of US drivers in the 1960s were asked: "Do you consider yourself an above average driver?" 93% said yes.

Investors, both professional and amateur, often take a similar view of their own investment prowess. Yet when it comes to forecasting, even the experts get it wildly wrong.

And therein lies the rub, since we like our 'experts' to sound confident. It is easy to be taken in by any number of claims, as long as they are made in a charming and confident manner.

In the words of the famed economist, J. K. Galbraith, "The only function of economic forecasting is to make astrology look respectable."

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