KENNEDY BLACK
WEALTH MANAGEMENT

QUARTERLY PRIVATE CLIENT NEWSLETTER ISSUE 20: DECEMBER 2014

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

I'm pleased to report that there's only a little bit in this edition about pensions. Just a little bit.

The focus this quarter is on some more general topics. The Autumn Statement was impactful in relation to the property market, but slightly disappointing on the pension front where we had hoped for more details. This edition also marks the final snippet on behavioural finance.

But following an interesting meeting with two new prospects recently, I wanted to touch on something far more important – what is financial advice (or 'financial planning'), why is it valuable and hence why is it worth paying for?

WHAT CONSTITUTES *GOOD ADVICE?*

Two interesting meetings recently have touched on similar points, and I felt that the answer was important enough to warrant a more detailed explanation in our newsletter.

These conversations boiled down to the same two questions: What is advice? And is it worth paying for?

Both conversations were with new clients where the starting point was an investment portfolio. And in both cases the conversation moved onto the service that Kennedy Black Wealth Management delivers to its clients and the fees we charge.

Our service is a premium, face-to-face, bespoke, financial planning service that encompasses all elements of our clients' affairs. We help clients define their goals and ambitions (to be developed further in future editions of this newsletter), understand where they are – often in the middle of a complicated mess – and help put a defined and, hopefully, disciplined plan in place to reach those goals. We ensure everything is structured tax-efficiently and we take care of a lot of the boring stuff - e.g. corresponding with pension companies.

The goals bit is often over-looked. However, in our view, talking about goals in an abstract sense is somewhat meaningless, so I'll jump the gun and give you a quick sneak preview of the next couple of editions of this newsletter by suggesting two 'goals' that we like to use with clients. Often this is the first time they start thinking properly about why they get up in the morning:

1. *Financial independence* – where work is optional and you can relax in the knowledge that your current lifestyle is affordable for the rest of your life without the fear of running out of money.

2. *A retirement of your making* – involving spending time travelling or with friends and family, instead of stacking shelves at the local supermarket to pay the bills.

If you're anything like our typical client, you're probably nodding along to both of those points, thinking: "That sounds good."

A good financial adviser can help you identify the goals that are important to you, address the various facets to your financial existence, make sense of everything and demonstrate what you need to do in order to get where you'd like to be.

While part of that process may involve the use of investments, in our experience, the investments form a very small part of what we do with and for clients.

To focus on just the investments essentially means all you think you are paying for is "fund picking."

Financial advice is not, and should never be, solely about fund-picking. Whether you believe in the abilities of star fund managers or not (we don't), anyone can pick funds. In fact, it turns out even monkeys can pick funds and be rather good at it (see the book "Monkey With A Pin" by Pete Comley).

A lot of companies will tell you they can pick funds. Some claim to do it cheaply (although we often find it is worth digging a bit more deeply to understand exactly what how much you will be paying and what for). And people often think they can do it themselves.

The point is, if you're not getting *independent and comprehensive advice* with that, then you're missing the bigger picture. You may not be properly optimising your tax position (e.g. forgetting about Inheritance Tax?) nor understanding *why* you're investing in the first place.

Recent research from Vanguard, the US passive fund manager, has identified five key areas where advisers can add the most value. It is interesting to note that 'picking funds' isn't on the list:

- Constructing a sensible, broadly diverse asset allocation model;
- Annual rebalancing;
- Reducing costs elsewhere – e.g. through access to institutional funds;
- Behavioural coaching (see the column on the right);
- Effective use of tax wrappers and allowances;
- A sensible spending strategy;
- Focusing on 'Total Return' rather than 'investing for income' (something I rounded against in issue 15)

In total, Vanguard estimates that these benefits add up to a quantifiable 3% a year.

Personally, I think the behavioural coaching element is worth considerably more than this in its own right. A recent academic study of DIY investors in Germany (Meyer, Schmoltzi et al, 2012) found that 91% under-performing the market, on average by 8.5% a year after fees. You might be smart, well-educated, and financially literate, giving you a good chance of being better than average, but frankly the average stinks.

Our aim is therefore to build a robust and disciplined process based on an appreciation of human behaviour, thereby improving the chances of a successful investment outcome.

The Autumn Statement

In case you missed it, it was the Autumn Statement last week. George Osborne bravely tore up the rulebook on Stamp Duty Land Tax. We are pleased to see the old 'slab' system consigned to the history books.

In short, the new tax is a combination of the following tiers:

0% on the first £125,000;
2% on the balance up to £250,000;
5% on the balance up to £925k;
10% on the balance up £1.5m;
12% on everything above £1.5m.

98% of house transactions are estimated to see a reduction in Stamp Duty. Properties of around £1m and more will see their tax bill rise (considerably, for properties of £3m and above).

The politics of it looking most interesting though, since a top rate of 12% looks a lot like a 'mansion tax.'

The Autumn Statement was a bit disappointing on the pension front, however, having been promised so much in relation the final wording of the new rules coming into force in April.

In particular, we were expecting much greater clarity on QROPS (Qualifying Recognised Overseas Pension Schemes) but this topic was omitted.

In other news, the NISA allowance will rise from £15,000 to £15,240 in April. Furthermore, NISA wrappers will no longer be extinguished when an individual dies and passes their NISA portfolio to their spouse. NB this isn't the same as protection from Inheritance Tax, which still applies to NISAs.

Irrational behaviour #10:

"Hindsight Bias"

The final behavioural bias in our series of ten is 'Hindsight Bias'. This is the innate tendency to look back on events and apply what we know now. As a result, people tend to overestimate their ability to have predicted an outcome that could not possibly have been predicted.

In a somewhat anecdotal example, customers of ING in the Netherlands were asked after the recent financial crisis whether, on reflection, they could feel the crisis was coming in advance. A surprisingly high 43% said yes. Only 27% said no.

What hindsight most consistently ignores is a feeling of uncertainty. In the present, now just as always, the future is uncertain. Yet when we reflect on times passed, we tend to forget the uncertainty – another example of the Empathy Gap (see issue 16).

It turns out that there's not much you can do about Hindsight Bias other than be aware of it and try to be more honest with yourself.

Kennedy Black Wealth Management Ltd • 41 Lothbury • London • EC2R 7HG
Tel: 020 7125 0224 • enquiries@kennedyblack.com • www.kennedyblack.com