

## INVESTMENT STRATEGY

Asset allocation – that is to say, the technique of spreading investments between different types of asset, including; equities, bonds, property, commodities – has for long been regarded as the key to reducing risk.

However, the dire markets of 2008 have led some people to question the established assumptions and to suggest that the only distinction to be made is between risky assets and (relatively) risk-free assets.

It used to be assumed that cash was a risk-free asset but many savers were disabused of this assumption when Northern Rock hit the buffers. Government bonds were regarded as the ultimate safe asset, but the futures market has suggested that with massive borrowings even this assumption might be questioned.

During the last century Governments - including UK Governments - effectively reneged on their obligations by printing money and letting the resulting penal levels of inflation reduce their debt burden.

War Loan, the Government borrowing which was designed to appeal to people's patriotism as a means of funding the cost of the first world war, was a classic case in point. Its capital value declined to pitiful levels as a result of inflation, causing commentators to refer to this stock as a Guilt-edged security.

Although inflation is detrimental to paper assets, it does favour investment in physical assets, classically bricks and mortar, though the downside in values can be as impressive as the upside when the pendulum swings.

Some storm-tossed investors have considered following the French tradition of keeping cash under the mattress, and the boom in sales of home safes suggests that this is a risk some people are prepared to take.

"Moderation in all things" was the maxim of one of Galsworthy's characters, and this should be an investors' guiding principle.

All risk is relative, and in relative terms the current extreme financial climate clearly favours a balance which is weighted towards cash and fixed interest securities, particularly where shorter term investments are concerned.

However, growth opportunities will inevitably become available, the likes of which, according to one fund manager reported in the Financial Times, "we've never seen before".

Commentators are suggesting that following the surge of the gilt market in the second half of 2008 as investors sought a safe haven, the next sector to recover will be the corporate bond market; and it must be a positive sign that the particular sector of the bond market currently receiving attention is convertible bonds, which offer both a fixed rate of interest and the option to convert to equities at a future date.

Whilst any downturn, especially the current one, is uncomfortable for investors, it reiterates the need for a robust risk profiling and asset allocation process which takes account of the investment time frame rather than seeks to call short term swings in markets.

## PENSION LIMITS

The Government, in its pre-Budget report, has stated its intention to reduce the sums which can be invested in pensions and benefit from tax relief. The reduction applies both to annual contributions and to total accrued values.

It had been anticipated that both the 'Annual Allowance' and the 'Lifetime Limit' would increase in line with inflation, but now they are to be frozen from 2011 to 2016.

The limit for annual contributions will be 100% of salary, capped at £255,000, and the limit on total accrued value will be frozen at £1.8m. In a final salary scheme this would equate to an annual pension of £90,000 p.a.

Those who had pension funds worth more than the "lifetime allowance" on 5 April 2006, when the limits were introduced, are able to apply to HM Revenue & Customs for the excess to be "protected", but must do so before 6 April 2009.



## TAX ON TRUSTS

Another announcement in the pre-Budget report related to the taxation of trusts. With effect from 2011, tax on savings income received by trusts is to be increased from 40% to 45%; and tax on dividend income is to be increased from 32.5% to 37.5%.

The increase will add to the attraction of holding trust investments in an Investment Bond tax-wrapper. When income is accumulated within a Bond it suffers tax at 20% or less, and if segments of the Bond are assigned to beneficiaries the gains are taxed at their personal rates – which clearly favours those paying tax at the basic rate or less.

## PERSONAL DIS-ALLOWANCE

In pursuance of the declared objective of ensuring that the better-off play their part in helping the Government out of its problems, the Chancellor also announced that from 2010/11 the availability of the basic personal allowance will be reduced by £1 for every £2 of annual income over £100,000; and for those with income over £140,000 p.a. the allowance will be further reduced until it is extinguished.

In addition, from 2011/12 income above £150,000 will be liable to income tax at 45% (the same rate as will apply to trusts).

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No responsibility can be accepted for the accuracy of the information in this newsletter and no action should be taken in reliance on it without advice.  
Please remember that past performance is not necessarily a guide to future returns.  
The value of units and the income from them may fall, as well as rise. Investors may not get back the amount originally invested

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