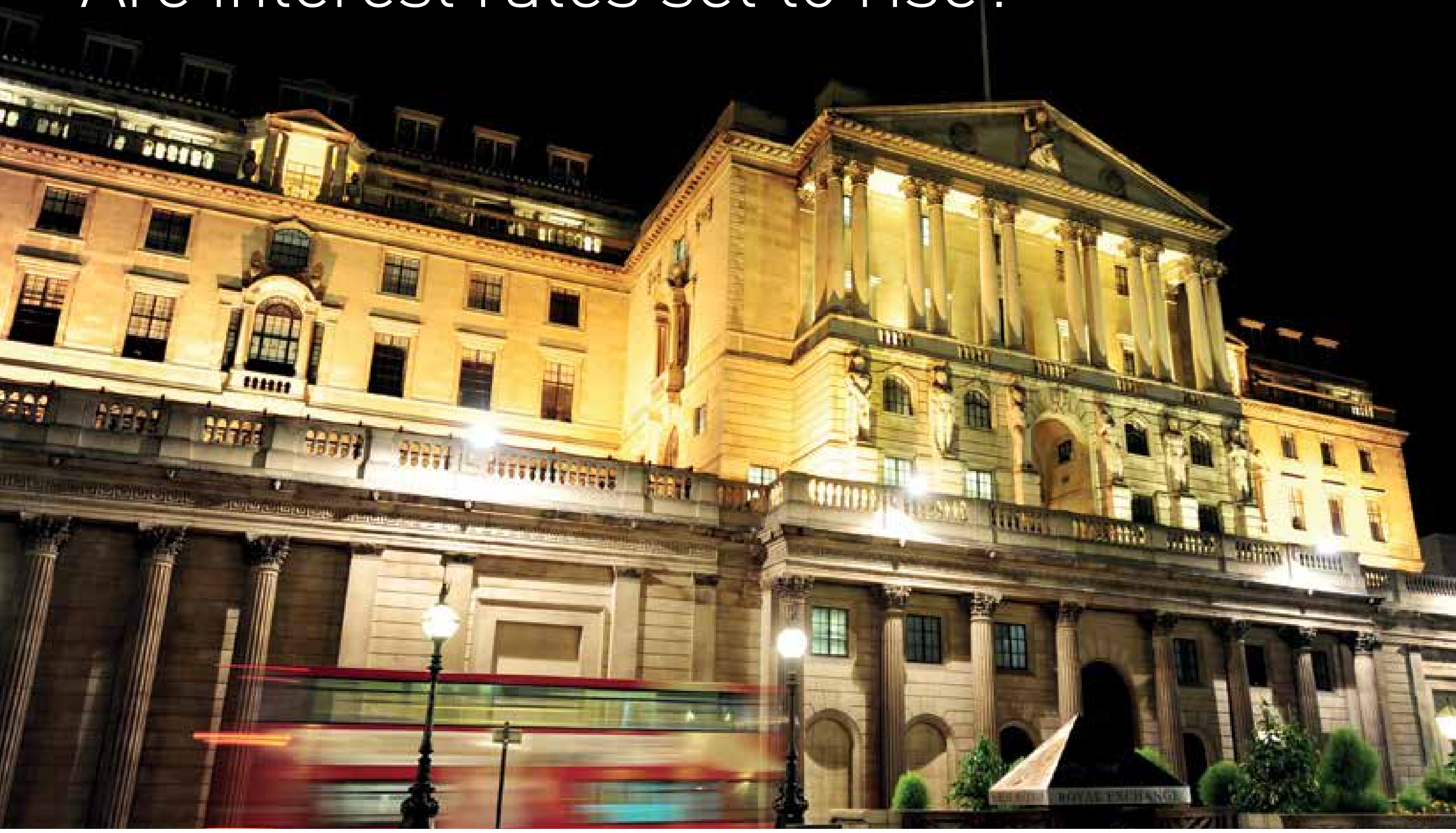
ASSET

THE NEWSLETTER OF MURDOCH ASSET MANAGEMENT

SEPTEMBER 2014

Are interest rates set to rise?



UK employment rose by 345,000 between February and April – the biggest increase since records began in 1971 – but the unemployment rate only fell from 6.8% to 6.6%, which means that new entrants to the job market made up 61% of the increase.

Consumer Price Inflation rose briefly to 1.9% in June before falling back to 1.6% in July and 1.5% in August. GDP returned to its pre-crisis level, with the annual rise estimated to have been 3.1%. The improved economic activity is very welcome, however as 1 million more people are in work and contributing to this rise, it means that we are far less productive per worker than before. It also explains the downward pressure on wages and why working people feel poorer.

The Governor of the Bank of England, Mark Carney, has warned investors that the first interest rate increase "could happen sooner than markets currently expect", which is an odd statement given that a rise has been expected since mid 2009, three months after hitting the current level of 0.5%. The timing of an increase is as hard to predict as ever but we can be pretty certain it will be many years until the heady days of 7% interest on a deposit account will return. (continued on back page)

IN THIS ISSUE

In this issue we look at rising employment and its impact on the market, and we give our views on predictions for interest rate rises. We also explain HMRC's introduction of tax increases for multiple discretionary trusts and look at how changes to IHT rates can mean a significant benefit for good causes.

Fund Manager news

The CF Woodford Equity Income fund officially launched on the 19th June raising over £1.6 billion during its initial public offer period, eclipsing the £460 million record formerly held by the Fidelity China Special Situations investment trust. Neil Woodford's new venture has continued to attract further inflows, growing to over £2.4 billion by the end of July 2014.

As a consequence of our monitoring service, we made two meaningful changes to our portfolios over the past quarter. We switched out the TM Cartesian UK Opportunities fund in favour of the Standard Life UK Equity Unconstrained fund, managed by Ed Legget. We have been monitoring Ed for a while and felt that the time was right to move out of the Cartesian fund – a product we supported when it launched in December 2005.

The other notable change has been within our income portfolios, where we moved out of the Newton Global Higher Income fund in favour of our existing funds. We started buying the Newton fund to provide us with diversification from UK and European equities for income. The fund did this job well but over time we have been able to introduce more regions of the market, including the US and emerging markets. These additional assets meant that the benefit of the Newton fund was reduced and we decided to move all existing holders out of that fund and into alternatives.

We will be recommending that investors switch away from the Old Mutual UK Smaller Companies fund as its large size has lead to a degree of mediocrity of late. It is being replaced with Anthony Cross's Liontrust UK Smaller Companies fund – a smaller and more nimble fund, which has a good track record.

Much ado about discretionary trusts

The taxman has stealthily introduced a tax increase for those who create multiple discretionary trusts as a way of reducing the periodic and exit charges on the value of large trusts. Marketed by HMRC as simplification, it has clamped down on this strategy – known as 'Rysaffe planning' – and will limit the amount that can be transferred into multiple trusts free of tax. This means that more tax will be payable in the future, however in practice it will only apply to the very wealthy.

A periodic charge is levied against a discretionary trust every ten years in the form of an effective tax rate of 6% on everything above the nil rate band (currently £325,000). If money is distributed from a trust after a periodic charge has been made, a proportional exit charge also applies. Under existing rules, trusts established on different days have their own nil rate bands and if several trusts have been established to receive an entire estate after the death of the person who set them up, there are significant inheritance tax savings.

HMRC advised that as from April 2014, all discretionary trusts set up by one person should have one Settlement Nil Rate Band (SNRB) split across all of them, with the periodic charge calculated for the trusts in total rather than for each individual one when it reaches its periodic review. This means that creating multiple 'pilot' trusts will no longer achieve inheritance tax savings.

All in all, moving to a flat rate charge will greatly simplify the calculation of periodic and exit charges.

A person can still set up a discretionary trust of up to £325,000 every seven years without incurring the 20% initial charge on the combined total and can decide what proportion of their SNRB to attribute to each of them.

All in all though, moving to a flat rate charge will greatly simplify the calculation of periodic and exit charges, with sound lifetime trust planning continuing to achieve considerable benefits, so it's wise to take action now if you want to reduce your children's inheritance tax burden.

Positive feedback

As part of our commitment to the very best service, we make a point of asking our clients what they think of us so that we know if we are succeeding or where we can improve.

In a survey completed by 30 clients at our recent client conference, we scored an overall 93% satisfaction rating. We asked:

- How effective are we at meeting your needs? 96.5%
- How easy is it to work with us? 96.43%
- How enjoyable are your interactions with us? 100%

Will the British become the new philanthropists?

Making a charitable donation from your estate means that your children will get a little less. However, government rules mean that your chosen charity will get a lot more.

Under rules introduced in 2012, if 10% or more of a chargeable estate is left to charity, then the inheritance tax rate of 40% is reduced to 36% on the remainder. Whilst this inevitably reduces the amount of money your children will inherit, it substantially increases the amount of money going directly to the charities that you have nominated.

The following is an example of how this works in practice and clearly shows why a charitable bequest makes a great deal of sense.

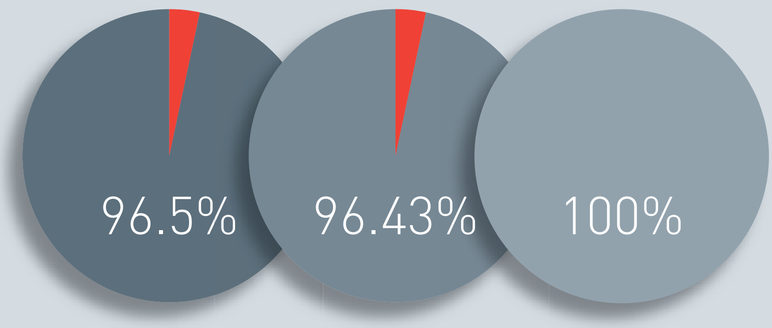
	Without a charitable bequest		Adding a charitable bequest
Property	£725,000	Property	£725,000
Investments	£406,000	Investments	£406,000
Cash	£70,000	Cash	£70,000
Total	£1,201,000	Total	£1,201,000
Nil rate band	£325,000	Nil rate band	£325,000
Chargeable estate	£876,000	Chargeable estate	£788,400
IHT at 40%	£350,400	IHT at 36%	£283,824
Net to children	**£850,600**	**Net to children**	**£829,576**
		Charitable Bequest	£87,600
		Total	**£917,176**
		Tax saving	**£66,576**

Setting up a charitable bequest is straightforward. You won't need to rewrite your will as a bequest can be added using a codicil – a simple sheet of paper signed by you and witnessed then stored with your will. The charity that you want to leave a donation to may be able to provide you with a ready-prepared codicil for you to complete and if you'd like us to help, please get in touch.

If 10% or more of a chargeable estate is left to charity, then the inheritance tax rate of 40% is reduced to 36% on the remainder.

We also asked clients to rate our advisory service and ongoing administration on a scale of 1-5 and we scored 4.6 and 4.52 respectively.

We were pleased with the results but we don't intend to rest on our laurels and will be working even harder towards improving our rating. Our current projects include an improved Client Hub, increasing the investment committee to nine members and a more comprehensive annual review pack.



How effective are we are meeting your needs?

How easy is it to work with us?

How enjoyable are your interactions with us?

Staff update

We are very proud of our culture of continuous learning and the high industry and academic qualifications that our staff hold. In recent months, many of them have added to their achievements.

Photos, l-r, Mark Collard, Marie Dinsdale, Austen Robilliard, Margaret Andrew, Lisa Flynn

Mark Collard has begun working towards the Diploma in Regulated Financial Planning and has passed the exam in Integrated Financial Planning.

Austen Robilliard has passed the UK Regulation & Professional Integrity exam as part of the Investment Advice Diploma.

Sarah Thomas has passed the Financial Services, Regulation and Ethics exam as part of the Diploma in Regulated Financial Planning.

Marie Dinsdale is working towards the Certificate in Financial Planning and has passed two exams – Investment & Risk and Financial Protection – with two more to go to complete the certificate.

Lisa Flynn has passed the Financial Services, Regulation and Ethics exam as part of the Certificate in Financial Planning and is similarly two exams away from completion.

Margaret Andrew has passed the Platform Services exam towards the Certificate in Financial Services and has one final exam to pass before completing.

Philip Hunt has passed the Investment Principles & Risk exam as part of Fellowship of the Personal Finance Society. This is the highest possible qualification from the Chartered Insurance Institute and Philip has now achieved 320 of the 350 required credits.

Samantha Cross, who joined us in February this year, has gained a Level 3 Certificate in Investment Administration. She has also passed the Pensions and Retirement Planning exam as part of the Diploma in Regulated Financial Planning and the Investment and Risk exam towards the Certificate in Financial Planning.

On a different note, Sarah Thomas has moved to the financial planning side of the business and joined the investment committee in order to pursue her keen interest in pensions and investment.

(Are interest rates set to rise? continued) The US continues its recovery with the S&P stock market index returning 4.17% over the past 3 months, ahead of European equities, which were down –1.88% to the end of August this year. Emerging markets rallied strongly, with the Index up 9.83% and Asia Pacific (ex Japan) up 9.58%. Indian equities have risen an impressive 24.10% and the FTSE Gold Mines Index Series is up 24.35% year to date; although it has a long way to go before recovering all of its 2013 losses at –52.25%.

Low European inflation, poor economics and the risk of deflation forced the European Central Bank to reduce its main financing rate from 0.40% to 0.15% in an attempt to boost demand and stave off corporate defaults. The Deposit Facility Rate changed to –0.10%, encouraging banks to lend or pay charges for holding on to cash. Time will tell how this pans out but the Ukrainian situation and trade sanctions between Russia and Europe are not helpful.

Last year's emerging market currency depreciation has been steadily reversing, rewarding emerging market government debt investors. There has been some share price recovery in the Investec fund of 6.42% in the last six months, with interest rate yields on offer at 6.43%.

The Japanese Topix index soared 54.41% as the Bank of Japan stimulated export demand by depreciating the Yen, leaving UK investors in Japan making only 24.67% once the currency effect was accounted for. We remain uncomfortable with Japan because of the fundamental 'strength' of companies in this region and we don't like taking bets on short-term currency fluctuations.

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