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NEWSLETTER

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It's plain sailing...

Interest-only mortgage holders may 'face repossession'*

The Citizens Advice Bureau has warned that almost a million people have no strategy in place for repaying their interest-only mortgage and could face repossession.

Research from the charity estimates that 934,000 people have an interest-only home loan and do not have a plan for how they will pay it off when it matures. That is much higher than a previous estimate issued by the Financial Conduct Authority (FCA) in 2013, which put the number at around 260,000.

The Citizens Advice Bureau said that time is running out for some homeowners who would either have to sell their home, find the money to pay off the debt, or risk having the property repossessed.

Its research represents the latest in a series of warnings about interest-only mortgages, which have helped millions of people onto the housing ladder during the past two decades, but have in recent years become the subject of a regulatory clampdown.

In 2013, the FCA published research showing that up to 2.6m interest-only mortgages will mature by 2041, of which almost half of the homeowners may be unable to repay the loan at the end of the term. However, 90 per cent of the borrowers said they had a repayment strategy in place to repay what they owed.

The Citizens Advice Bureau research, which included a YouGov poll, suggests the regulator may have underestimated the scale of the problem. It puts the number of people holding interest-only mortgages at 3.3 million. The charity said that figure included 1.7 million who said they had no linked repayment vehicle, such as an endowment or ISA, and 934,000 who had no strategy for repaying the loan. More than 430,000 people "have not even thought about how they will repay the capital," it said.

*Your home is at risk and may be repossessed if you do not keep up the payments.

Views sought on new Inheritance Tax Proposals

Earlier this year during the Summer Budget the Government announced it would phase in a new residence nil-rate band (RNRB) from 6 April 2017 when a residence is passed upon death to a direct descendant.

This has been designed to reduce the burden of Inheritance Tax (IHT) by making it easier to pass on the family home to direct descendants without a tax charge and has been seen as a response to the UK's growing house prices.

When phased in the rates will be:

- £100,000 in 2017 to 2018
- £125,000 in 2018 to 2019
- £150,000 in 2019 to 2020
- £175,000 in 2020 to 2021

After this initial planned period, rates will then rise in line with the Consumer Price Index (CPI) from 2021 to 2022.

However, in a new technical note, HM Revenue & Customs (HMRC) has announced new proposals to take into account people who choose to downsize to a less valuable property later in life or who cease to own their own home, to ensure that they are not unfairly penalised by the policy.

In its note, HMRC said: "The Government recognises that individuals may wish to downsize to a smaller and often less valuable property later in life. Others may have to sell their home for a variety of reasons, for example, because they need to go into residential care.

"This may mean that they would lose some, or all, of the benefit of the available RNRB. However, the government intends that the new RNRB should not be introduced in such a way as to disincentivise an individual from downsizing or selling their property."

It goes on to say that where part or all of the RNRB might be lost because the deceased had downsized to a less valuable property, or had ceased to own a residence, the lost RNRB will still be available as long as a number of qualifying conditions are met.

State pension top-ups 'window' opening soon

The government has issued a reminder that for a limited period starting in October, certain people will be able to make extra national insurance contributions to top up their state pension.

Between 12 October 2015 and 5 April 2017, men born before 6 April 1951 and women born before 6 April 1953 will be able to make Class 3A voluntary contributions to boost their pension by between £1 and £25 a week.

The government has created a calculator so that someone can work out how much they will need to contribute as a lump sum, based on how much extra pension they would like to receive and their age when they make the contributions.

For example, the contribution required for an extra £1 pension per week for a person aged 65 is £890.

This means that for £4,450, they could receive an additional £5 a week, or £260 per year for life, increased in line with prices and inheritable on death in the same way as existing additional state pension, with a minimum of 50 per cent for their spouse or civil partner.

However, this may not be the best course of action when you take a closer look at the figures. The additional income you would gain is an extra £260 p.a. and assuming you are a standard rate taxpayer, this will reduce to £208 a year after tax is deducted. Alternatively, if you do not put the additional £4,450 'top up' into your pension and invested it and achieved say 3.5 per cent Net Growth on the capital, it would be 27 years before you were worse off even if the pension was increasing by 2 per cent p.a. Even assuming you only achieved 1.5 per cent Net Growth on the capital the breakeven point would be around 21 years. Although most people want to improve their pension income, this may not be the best way to achieve it. Therefore, if this is something you were considering, please feel free to contact your adviser to discuss the options before making any final decisions.

Buy-to-let bubble could burst*

Following a recent report that highlighted buy-to-let (BTL) mortgage deals were at a seven-year high, the Bank of England has warned that this boom potentially poses a risk to the UK's economic stability.

The Bank's Financial Policy Committee (FPC) warned that landlords, typically funded through interest-only loans, could be "disproportionately vulnerable" to large falls in house prices and could in turn amplify any future property downturn.

Data shows buy-to-let mortgage lending has risen by 40 per cent since 2008, 20 times faster than owner-occupier loans. In the same period, the buy-to-let share of the market has risen from 12 per cent to 16 per cent with more people than ever before renting privately.

This concerns policymakers because a continued increase in the market risks pushing up house prices further, meaning more borrowing and greater household debt. If landlords see their loan repayments starting to exceed their rental income, they may respond by selling their property, resulting in an accelerated downturn in the property market.

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Market Report

25 September 2015

Global Review

Global financial markets have been dominated by events in China where, after a strong rally in the first half of the year, equities sold off heavily following a series of weaker economic data releases and a surprise move by the Chinese authorities to devalue the yuan. The falls in China were quickly mirrored across the globe as investors moved to reduce risk. Sentiment was already subdued by speculation over the timing of US interest rate rises and the increasingly desperate efforts by the Greek government to agree the terms of a bailout package with the country's creditors.

With many developed markets peaking at post-Financial Crisis, and in many cases new all-time, highs in the first quarter, the falls in equity prices have left most markets flat year-to-date. Asian and Emerging Markets have struggled after a strong first quarter as concerns over growth in China, the region's largest economy, together with the prospects of higher borrowing costs has undermined local currencies as well as equity markets. The recent turmoil has postponed any potential interest rate rises as central banks remain cautious.

UK

The FTSE 100, an index of the UK's largest companies, fell back below 6,000 in the aftermath of the sell-off in China after peaking at over 7,100 in April. Mining and Oil stocks have been notable drags on the index as the global demand for commodities has waned and concerns over the slowdown in China has exacerbated the problem. The price of oil has fallen to below \$50 per barrel after trading at over \$115 per barrel just 12 months ago. Whilst falling input costs are considered positive for global growth over the longer-term, these moves do have a significant impact on equities in the short-term.

The preliminary estimate from the Office for National Statistics suggests the UK economy expanded at a rate of 0.7 per cent in the second quarter, the tenth consecutive period of positive growth. Year-on-year growth has been 2.6 per cent and GDP is now estimated to be 5.2 per cent higher than the pre-Financial Crisis peak. This has placed additional pressure on the Bank of England to raise interest rates from 'emergency levels' with both employment and wages also rising. The Bank however are mindful of stubbornly low inflation numbers and in solidarity with the US Federal Reserve are maintaining a near zero interest rate policy as events in China settle.

US

The US Federal Reserve, who were seemingly preparing markets for a first interest rate rise in September, have also delayed a hike following the China sell-off. In her latest statement, Fed Chairman Janet Yellen, argued that whilst the pros and cons of an interest rate rise are balanced, US economic growth and inflation are unlikely to remain unaffected by global events. The expectation now is that the Federal Reserve will move in December but again this will be data dependent with the bank likely to err on the side of caution rather than jeopardize the steady recovery.

US growth estimates for the second quarter have been revised sharply higher from an initial 2.3 per cent to 3.7 per cent, much higher than consensus forecasts. However, a strong rebound was expected after a slow first quarter during which the economy expanded by just 0.6 per cent due to extreme weather conditions. Unemployment has also continued to fall and now stands at just over 5 per cent. However, recent events have prompted the bank to revise down estimates for growth in both 2016 and 2017 as well as forecasts for employment.

Europe

The failure of Greece to reach an agreement with its creditors and the rejection of an extension for debt repayments beyond the June deadline prompted Prime Minister Tsipras to announce a referendum on whether to accept the current bailout conditions and continue with the imposed austerity measures. As a result the European Central Bank also froze the level of emergency loans to Greek banks causing their closure to prevent capital flight. Despite the real possibility that a 'No' vote would lead to Greece leaving the Eurozone, voters elected to reject the terms.

Mr Tsipras had hoped that a 'No' vote, an outcome he had campaigned for, would leave him in a stronger negotiating position. However, Eurozone finance ministers were not swayed by the result and Mr Tsipras was forced to accept even more stringent terms in order to secure a deal. Whilst the terms of the new bailout package and the required austerity measures were finally agreed by the Greek parliament, 32 members from the Prime Minister's own party opposed the bill. The unpopularity of the decision, clearly against the wishes of the electorate, prompted Mr Tsipras to call, but subsequently win, a snap election.

Japan

Prime Minister Abe has also won another three-year term as leader of the ruling Liberal Democratic Party in Japan and is now set to lead the country through to the next general election in 2018. Driven by the huge stimulus of 'Abenomics', Mr Abe's three point plan to revive the economy, the yen has fallen 30 per cent versus the US dollar and corporate profits have more than doubled. However, both corporate investment and wage growth have been disappointing with ramifications for both consumption and economic growth.

Economic output shrank by an annualized 1.2 per cent in the second quarter following strong annualized growth of 3.9 per cent in the first quarter. A similar fall in output during the same period of 2014 following a hike in sales tax resulted in a technical recession and prompted the Bank of Japan to expand its already aggressive stimulus plan. Despite calls for the government to address much needed structural reforms, the response is again likely to be more fiscal stimulus following the government's recent announcement on corporate tax cuts.

Asia

Chinese equities hit a seven year high in June before falling back sharply in the wake of disappointing economic news, the possible break-up of the Eurozone and an imminent interest rate hike in the US. Following the reform of equity markets last year, share indices have risen by up to 150 per cent fuelled by new private investors and a huge rise in borrowing that has enabled further participation in booming prices.

Better than expected second quarter growth of 7 per cent subsequently failed to halt the sell-off and the government have been forced into a number of measures to shore up confidence in both the economy and stock markets. State banks have provided additional funds to prop up markets and the People's Bank of China has devalued the yuan as well as cutting benchmark interest rates and the reserve requirement ratio.

Pensions freedom is six months old!

To mark the occasion the Association of British Insurers (ABI) has released its six top facts to emerge from the reforms. On 6 April 'Pension Freedom' gave the over 55s unparalleled access to their defined contribution pension funds, giving them the opportunity to release funds subject to their marginal rates of tax. People are no longer steered towards an annuity purchase as the reforms have opened up the income drawdown market to people with more modest pension funds and we have seen a surge in people accessing pension pot cash. Annuity sales have dropped significantly while income drawdown has increased.

Here are the ABI's six key facts:

- Interest in the reforms resulted in an 80 per cent increase in calls to pension providers in the first month.
- In the first three months, providers paid out almost £2.5bn in cash and income drawdown payments.
- About 60 per cent of all cash lump sums paid out in the first three months went to people younger than 60, and around 80 per cent to under 65s.
- For the same period, only 42 per cent of income drawdown payments went to the under 65s.
- In 95 per cent of cases where savers accessed a cash lump sum, they withdrew the entire fund.
- The amount of pension freedom cash withdrawn in the first three months represents less than 1 per cent of all pension funds held by over 55s.

ABI director of long-term savings policy Yvonne Braun said: "These figures show that tens of thousands of people have used the new pension freedoms so far to access money they have saved.

"There's been a lot of activity involving the under 65s, who account for more than four in every five cash lump sum withdrawals, but the majority of people have only been cashing in relatively small pots which account for a tiny proportion of all the money which could have been released.

"This shows that on the whole the British public are taking a sensible approach."

Dividend Allowance a 'back door' tax rise, say experts

The Association of Taxation Technicians (ATT) says guidance on the new Dividend Allowance will come as a "shock" to taxpayers.

Under current arrangements, basic rate taxpayers pay no tax on dividends received. Higher and additional rate taxpayers pay tax at 25 per cent and 30.55 per cent respectively on dividend income.

But in the Summer Budget on 8 July, Chancellor George Osborne announced that from April 2016, the existing system would be replaced with a new tax-free Dividend Allowance of £5,000 a year for all taxpayers.

The Budget document said: "This will ensure that ordinary investors with smaller portfolios and modest dividend income will see no change in their tax liability – and some will pay less tax."

In a factsheet on the allowance published on 17 August, HM Revenue & Customs said: "The Dividend Allowance will not reduce your total income for tax purposes. However, it will mean that you don't have any tax to pay on the first £5,000 of dividend income you receive.

"Dividends within your allowance will still count towards your basic or higher rate bands, and may therefore affect the rate of tax that you pay on dividends you receive in excess of the £5,000 allowance. You'll pay tax on any dividends you receive over £5,000 at the following rates:

- 7.5 per cent on dividend income within the basic rate band
- 32.5 per cent on dividend income within the higher rate band
- 38.1 per cent on dividend income within the additional rate band."

Michael Steed, president of the ATT, said: "As this measure was announced by the Chancellor as being a tax-free allowance it is understandable that taxpayers believed the dividend allowance would operate outside of an individual's tax rate bands.

"To now discover that the allowance is in fact restricting the amount of dividends that a basic rate taxpayer can currently receive without a tax liability is a fairly big shock.

"The Chancellor announced the dividend allowance as a positive measure for taxpayers but underneath it all it now appears to be designed as a tax-raising measure. Shareholders in family companies in particular may well feel that this is a tax increase by the back door.

"The limited examples provided in the factsheet suggest that some basic rate taxpayers may well have to pay more tax than under the current system whilst some higher rate taxpayers may actually pay less than at present.

"We are seriously concerned that the practical implications of the proposals have not been thought through thoroughly enough. We think there is an urgent need for detailed consultation in advance of the drafting of the relevant legislation so that it can be drafted appropriately taking the feedback into account."

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