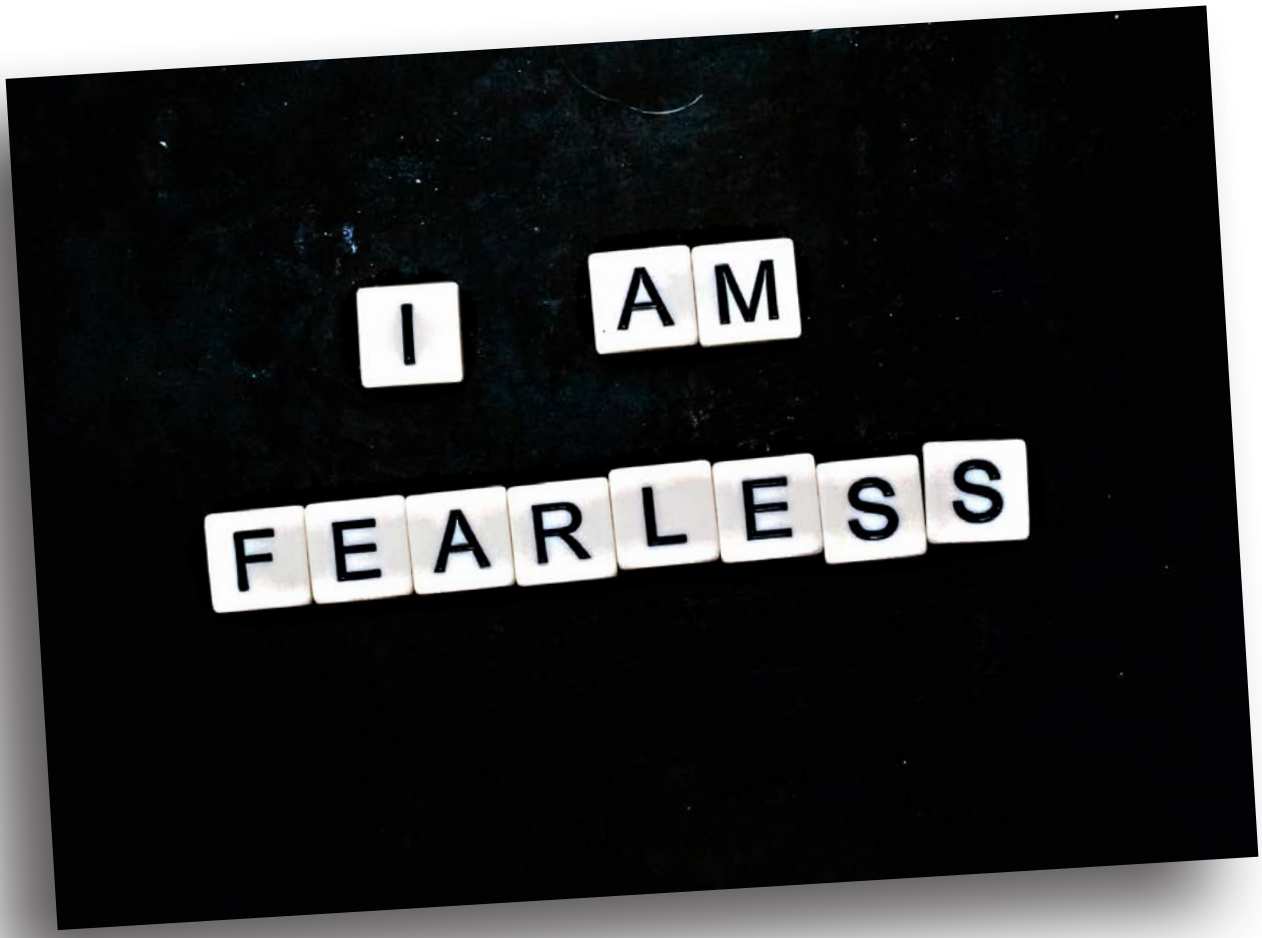
SEPTEMBER 2019

THE TRADE PRESS

The Federation of European Independent Financial Advisers



Risk perception

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Optimus Malta: planning for the future

Arnold Galea, Director of Optimus Malta.

"At Optimus Malta we are all about forward planning", says its Director Arnold Galea. "We look to get the foundations right and build long-term sustainable rewards from there. That's the model we seek to create for our pension clients, so it's only natural that we apply the same philosophy to our business."

The Optimus Group was founded in the Isle of Man almost 20 years ago and is responsible for client assets of around €1.5 billion across the full spectrum of corporate, trust and pension structures. Its first foray into the Malta pensions sector was in 2015, providing approved back-office services to a large QROPS scheme. Earlier this year, the group was granted a full Retirement Schemes Administrator Licence by the Malta Financial Services Authority.

This evolution has been ideal, according to Galea: "If you can't handle the administration demands of a pension, you most certainly can't cope with the fiduciary responsibilities. We have cut our teeth on administration in Malta over a few years now, working through a period of significant rule changes, plus we have almost 20 years of fiduciary expertise behind us too. Now we have brought these together and are really positive about the market that is opening up".

The market Galea refers to is about much more than just QROPS, as he explains: "QROPS was the staple diet for Malta-based pension providers for many years, particularly after 2012 when Guernsey's dominance disappeared almost overnight. After the latest round of changes in 2017, introducing the overseas transfer charge, Malta became the 'go-to' jurisdiction, albeit for a much more concentrated market. Good quality QROPS business is still out there, and we want it, but going forward the market will be much more diverse. Qualifying Non-UK Pension Schemes (QNUPS) have their place and are becoming better understood – as a group we have developed considerable expertise in their proper use and have seen some interesting and valuable applications.

"But the really interesting landscape is the broader one of international pensions. Starting with the EU, here we have a large bloc of countries where people move freely but fiscal systems are not aligned. Pension planning can be problematic in these conditions, particularly where employers have a workforce dotted around the EU demanding equal pension benefits. An EU-based international pension is most likely the answer and, in Malta, you get one which is well-regulated and relatively low-cost to administer. Plus, when the time comes to pay benefits across borders, the likelihood is that Malta's double taxation treaty network will be tax-efficient too".

When considering the market beyond Europe, Galea is just as bullish: "Fiscal borders exist everywhere and people are more global than ever in their approach to living, working and retiring. So, the same philosophy applies – you need a tax neutral international pension in a well-regulated country that is efficient to administer.

Whether across Europe, or across the world, demographic shifts mean that cross-border pension planning will be in ever-higher demand. However, we are not necessarily talking about the volumes that attract the cookie-cutter insurance companies – the IPP requirement is often more bespoke than that, and therefore suited to the independent players such as ourselves."

For now, Optimus continues with its business as usual demands whilst honing the next generation of products. This is all about customer outcomes, says Galea: "In the era of mass-marketed QROPS you would be forgiven for thinking that, all too often, the investment tail has wagged the pension scheme dog, often to the detriment of the customer. But we are now seeing a much greater focus on tying the two together. That's mostly led by the law makers and regulators, for example high profile judicial proceedings in the UK, MIFID II or even Malta's own overhaul of the investment aspects of pension planning. As trustees we must, quite rightly, take responsibility for customer outcomes – that is why one of our principal objectives is to develop high quality, sustainable relationships with professional, qualified investment advisers who can align closely with our responsibilities as trustee and administrator."

For further information contact Mark Schofield – Mark@OFL.co.im or tel: **+44 (0)1624 695 561.**

Editorial Comment

Conference time...

The *International Adviser* **Future Advisery Forum Europe** event takes place later this month, in London, on September 26th. In one guise or another this conference has now been running for 10 years and, once again, it is being held in association with FEIFA.

At the time of writing there are still a small number of places available at this event and also some complimentary hotel accommodation, although both are likely to run out very soon. If you haven't registered yet and wish to attend please click **here** as soon as possible.

The conference will be followed by the IA Awards and then by the FEIFA AGM.

I hope you had a great summer and, as always, that you enjoy the excellent and varied content in this issue.

Regards

Paul

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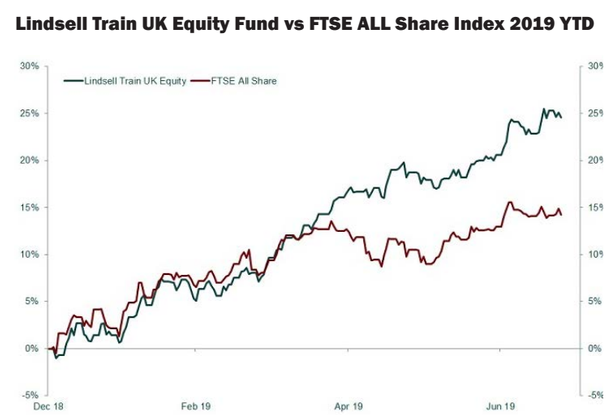
Process in action: this time is different?!

Nick Watson at Janus Henderson looks at the need for a blended and balanced approach.

All fund selectors can think of pure 'stock pickers', those portfolio managers (PMs) who are fixated on fundamental bottom-up company research and are wary about the idea of macro investing or asset allocation. Generally speaking, those strategies labelled as having a 'quality/growth' stance focus on really strong businesses with robust visible earning streams, defendable margins and high barriers to entry.

The 'stock pickers' will tell you that buying these steady compounders removes the macro, or market risk, from the equation. In theory, this may be the case. In practice, however, the market treats such an investment approach as a macro trade itself.

As a case study, let's take the performance of one of our highest conviction UK equity holdings – the Lindsell Train UK Equity Fund – over the period YTD in 2019.



Source: Morningstar Direct, 31 December 2018 to 24 July 2019.

Until mid-April, Lindsell Train was performing in line with the FTSE All Share index.

Pretty much every single asset rallied over this period, as risk appetite rebuilt across markets following the mass risk asset sell-off of Q4 2018.

Over this period, government bond yields stayed relatively flat as investors were not yet pricing in aggressive rate cuts from the Federal Reserve and further monetary stimulus from the European Central Bank.

Since mid-April, however, investment grade and government bond yields have collapsed, prompting yet another rally in fixed income prices.

No binary bets – our 'blended and balanced' approach

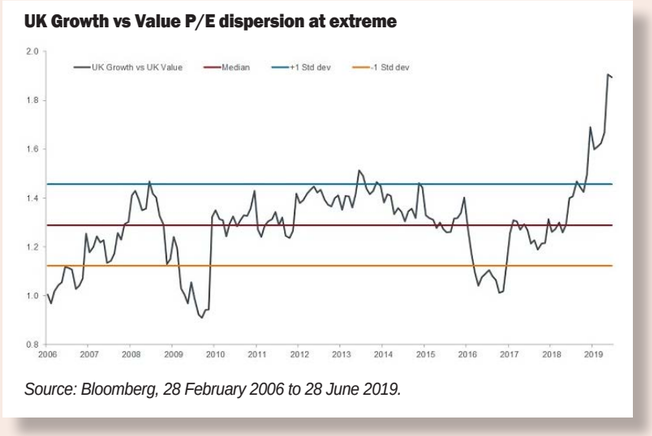
In terms of portfolio construction, we need to recognise the risks we are taking on behalf of clients. Whilst on the surface it may seem that holding quality/growth equities alongside investment grade bonds in the context of a balanced portfolio offers diversification given that they are different asset classes; the reality is that it is not very balanced at all. The two asset classes are the same bet on the same macro trend – specifically the cessation of the concept of an economic cycle and the establishment of a new paradigm of structurally lower growth and lower inflation in the decades to come.

In that macro scenario of "lower for longer", the UK 10-year Gilt yielding 0.7% would look attractive value and expensive quality/growth stocks would have the room to rerate even further. However, if underlying economic conditions change, causing yields to creep higher, not only will higher quality bonds deliver negative total returns but as a result, quality/growth equities would also be likely to underperform.

So where can we find attractive opportunities and diversification in this backdrop? The cyclical value PMs have suffered amid the market environment of the past decade. However, it is this value style that stands to benefit from any uptick in either economic growth or bond yields, whilst arguably offering genuine diversification within a balanced or multi-asset portfolio.

Despite the negative headlines, it is not hard to identify green shoots emerging from the already steady levels of global economic activity – a story that could argue for fewer rate cuts than the current dovish levels priced into bond and equity markets.

Given the potentially more constructive backdrop, investors are crowding into quality/growth trades, while the valuation gap between quality and value stocks continues to grow and is reaching extreme levels; all this despite stronger relative EPS (earnings per share) growth from those unloved value stocks.



Source: Bloomberg, 28 February 2006 to 28 June 2019.

Understanding how different assets, investment styles and instruments work together within a Multi-Asset portfolio is the primary responsibility of the fund manager.

Taking binary bets on the market backdrop is reckless risk management, so our approach is to seek out a blended and balanced approach that can be navigated through the market cycle to deliver attractive risk-adjusted returns in a wide range of market conditions.

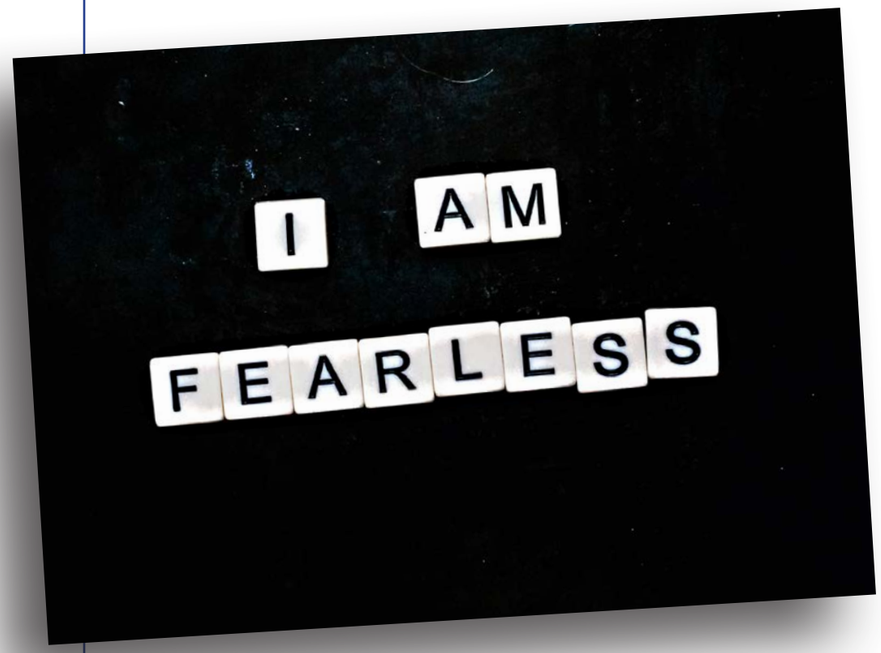
We are not arguing for a huge positive macro surprise prompting a sizeable mean reversion. There is an ongoing role for quality/growth equities within a portfolio and Lindsell Train UK Equity remains one of the largest holdings within the JH Multi-Manager Fund range. However, we have to recognise the strength of returns that quality/growth investing has delivered, driven in large part by the macro tailwind of falling bond yields. We want to build the rest of the portfolio to withstand and also take advantage of the winds of change, should the market regime of the past decade come to an end.

For information on our Multi-Asset Core Income range contact **David Firth**, Associate Director **– david.firth@janushenderson.com** or tel: **+ 44 (0)7960 455 734**.

Perception of risk:

strategies for coaching clients towards better composure

By Paul de Goede, Head of Technology, PortfolioMetrix.



We live in a "risky" world, (where "risky" is a lack of "certainty"). Everything we do has an element of risk and taking risk is a critical part of success in life. Risk is a necessary part of our journey and attempting to avoid all risk is a risk in itself. As we well know stuffing money under one's mattress or in a bank savings account is not a recipe for good retirement outcomes.

Delving into our perception of risk it becomes evident that we have evolved in ways that don't necessarily align with how our "risky" world currently functions. Evolutionary psychology gives us insight into biases rooted in our hunter-gatherer past. However, risk today looks very different. Our reaction to these risks however is millennia old.

Education about understanding and communicating risk is woefully inadequate. Risk is typically communicated in percentages. However, such a basic concept can be fundamentally misunderstood.

For example: there is a 30% chance it will rain tomorrow.

According to research published in the Bulletin of the American Meteorological Society in 2009, people have different interpretations of this statement:

- 30% of weathermen believe it will rain
- It will rain 30% of the hours in the day
- It will rain on 30% of the city or suburb they live in

With such diverse interpretations of a basic concept how can financial advisers effectively communicate risk, volatility and other complex concepts with their clients?

Being able to effectively communicate risk/benefit trade-offs to clients is key to the

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Income drawdown –your flexible friend

The thoughts of Paul Forman at Novia Global.

Those of us of a certain age will remember the credit card advertisement from the 1980's that used a tagline of 'your flexible friend' as a way of selling the need to have such a card in our wallets. The same can now be said of the flexible benefits regime that was created by the introduction of Pension Freedoms & Flexibility for UK money purchase pension schemes (such as International SIPPs) in the 2015 UK Budget.

What drawdown was permitted up to April 2015?

Previously, when not taking income by way of an annuity an individual could take drawdown in one of two ways: either by way of capped drawdown or a more flexible version, but both of these still came with restrictions.

Under **capped income drawdown**, the maximum amount of income that could be drawn was 150% of Government Actuary's Department (GAD) rates. Under **flexible income drawdown**, there was no limit on the amount that could be drawn from the fund as income but you had to evidence alternative secured income of at least £12,000 a year to be able to use this method.

What rules now apply to drawdown plans since April 2015?

From April 2015 all new drawdown arrangements have been classified as "flexi-access". Just like the previous capped and flexible drawdown options, the earliest age you can take scheme benefits is 55 (or possibly earlier if in serious ill-health). However, now you do not have to meet any of the pre-April 2015 restrictions for capped and flexible drawdown. In practice, this means you can take out as little or as much as you want from the accrued pension fund.

However, if you do start to draw funds but continue or commence building up UK pension benefits elsewhere there will be a change in the Annual Allowance rules pertaining to tax-relived contributions. The standard Annual Allowance is capped at £40,000 gross per annum but in these circumstances a reduced Money Purchase Annual Allowance (MPAA) applies. Originally capped at £10,000 pa the MPAA was reduced to £4,000 pa on contributions from April 2017.

Via flexi-access drawdown arrangements, you will be able to take 25% of the funds as a Pension Commencement Lump Sum (PCLS) at outset. You can also elect to take PCLS and at the same time defer taking an income for the time being or alternatively until you need to draw down payments at a later date. When deciding to draw income, all of it will be subject to UK income tax at marginal rate of income tax via the PAYE system. The Budget changes that same year also introduced a new type of drawdown product with a name that just rolls of the tongue - Uncrystallised Fund Pension Lump Sum (UFPLS). Under this type of arrangement, you do not take the full scheme 25% lump sum payment up front. Instead each time you draw down a payment from the scheme, 25% of this will be deemed to be a PCLS and the remaining 75% of each payment will be classed as income and is potentially subject to UK income tax at marginal rate.

As you can see from above, an International SIPP is under-pinned by UK pension legislation that offers a comprehensive range of retirement benefit options for expats and compares very favourably to QROPS in comparison whereby schemes in Gibraltar still operate on a restricted capped drawdown basis and Malta where there is no access to PCLS flexibility and the UFPLS option.

For further information contact **Chris Skelhorn – Chris.Skelhorn@novia-global.com** or tel: **+44 (0)7525 767 290**.

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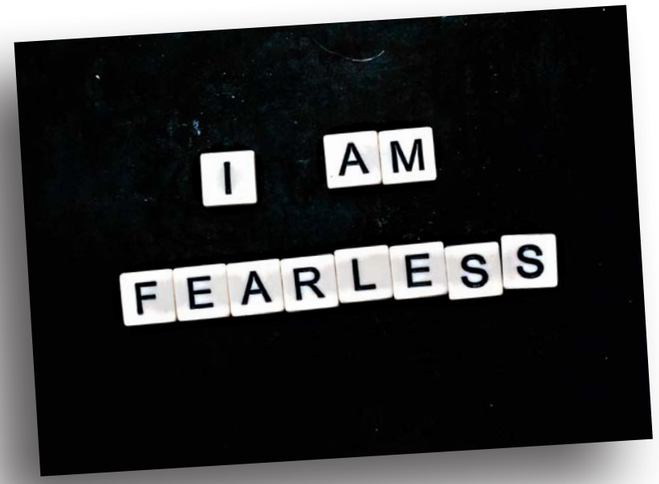
Perception of risk: strategies for coaching clients towards better composure

success of their investment strategy. The "trust me I'm a doctor" approach is not enough. Whilst trust in one's adviser is paramount; advisers need to engage clients in potential trade-offs that revolve around risk.

To unpack "risk perception" we must dig deeper into the human psyche.

Boiling Frog

A major unexpected risk event generates a disproportionate client reaction when compared with many minor risk events. People who chose to drive rather than fly post 9/11 increased their mortality risk by almost 100 times. A single and often short-lived market event generates more anxiety for advisers to manage than three years of muted returns.



Base Rate Fallacy

Simply put, people regularly ignore statistics in lieu of their beliefs, which are influenced by news, life events and their social environment. If a person is told they have a 5% chance of dying in a road accident many will interpret this as: "I'm a very aware driver so it's more like 1% for me".

Risk framing

People are far happier embarking on a treatment regime if it's framed as saving lives rather than preventing death. A "longevity chart" allows more positive engagement than a "death chart"! Positive framing of options will greatly increase people's choice.

Analysis paralysis

Like the proverbial "deer in the headlights", when someone is overwhelmed with choice, they tend to keep the status quo rather than make a decision. Which is why default portfolio selection for pensions is so important.

Advisers who are aware of these biases can educate clients about their responses to events, fostering positive client engagement and driving behaviour leading to better long-term investment outcomes.

For further information contact **John Croft – john.croft@portfoliometrix.com** or tel: **+44 (0)207 965 7533**.

Time to break up?

The honeymoon for US tech giants may be over, but is it time to break up? Chief investment officer Julian Chillingworth discusses the intensifying antitrust scrutiny of America's tech titans and how their future may rest on political machinations.

Just like other life-transforming technologies of the past, today's tech giants are making that inevitable transformation from fresh young face of innovation to overgrown, mistrusted hulk. Telltale wrinkles appeared in May amid reports that US antitrust bodies would be investigating Alphabet, Apple, Amazon and Facebook's competitive practices for possible violations.

Their share prices took a hit as investors feared a growth-busting breakup of these behemoths. So should you be concerned about exposure to these tech giants in client portfolios?

We've been talking about this inevitable development in our InvestmentInsights publication over the past year, in a series called 'The great tech breakup'. First we looked at the *history of antitrust in America*, and that didn't suggest bust-ups of the big US tech firms were imminent; or the end of the road for these businesses even if breakups did come. But we don't doubt that they'll see more volatility in the short term.

The taste of freedom

A century ago America was waking up to the tremendous freedom and opportunity provided by the internal combustion engine. Oil was the lifeblood of the new economy of the 20th century, and increasingly controlled by John D Rockefeller's Standard Oil.

Today social media and the internet are radically changing how we communicate, transact and live. Today's quality data is pivotal and increasingly concentrated in the hands of a few tech giants. Standard Oil was found to be abusing its power, and was split up by the government in 1911 after taking its case all the way to the Supreme Court. They broke it up to ensure competition reigned supreme in America. Could the same happen with today's tech titans?

First we need to ask, why does new technology eventually attract the controlling gaze of state regulators? There's a tipping point where a luxurious new gadget or service becomes so ubiquitous that it's seen as a de facto right. There was a time — not so long ago — when indoor plumbing or electricity were beyond the reach of many Americans and Britons. Now it's unthinkable to let a home or office be without them. Should we now add internet access to that list of required amenities?

The trouble is, today's high-tech businesses, with their complexity of design, operation and business models, make antitrust law — which is always evolving and depends ultimately on the view of the Supreme Court — difficult to apply. That's something we explored in *part two of 'The great tech breakup'*. In more recent antitrust history, Microsoft continually clashed with the government. It eventually settled in 2001, and agreed to be more open with its software and coding in return for remaining intact as a business. It then languished in the doldrums for a decade before re-emerging as a tech giant once again.

Even if one or more of Microsoft's younger rivals are broken up, there is hope for investors that the sum of the parts may be worth more than the whole. When Standard Oil was split into Exxon, Mobil and Chevron, the combined growth of these businesses easily eclipsed their predecessor. You could say it was win-win: Mr Rockefeller got richer and America got a free and competitive oil market.

For antitrust breakups to happen two things are required: the government has to push for it and the Supreme Court has to have a sympathetic ear. America's top court is the final arbiter of antitrust law, as we noted in the conclusion of *'The great tech breakup'*. President Donald Trump has been vocal about wanting to rein in tech companies. But the court has tacked significantly to the right after Trump's appointment of Neil Gorsuch and Brett Kavanaugh.

Will US tech giants survive the coming years unscathed? That depends on political machinations, both at home and abroad, and the economic beliefs of two greenhorn Supreme Court Justices. Some new technology may come along to eclipse them, but we doubt they'll be going extinct any time soon.

For further information contact **Chris Wanless – Chris.Wanless@rathbones.com** or tel: **+44 (0)207 399 0238**.

Where do financial advisers stand today?

The thoughts of Moneyrebel.

In recent years all financial service providers have been facing an unprecedented array of challenges. Shrinking revenues and intense pressure from clients and regulators demand the adoption of new business models. That's why we are witnessing huge steps toward mobile, AI and other new technologies. There are new players and FinTech firms, which have emerged to challenge traditional financial institutions and advisers. Digital is becoming more and more important to clients, who place the highest value on protection and personal financial management (PFM), followed by mobile payments and the personalized digital experience. These concepts come well above widely publicized FinTech concepts such as peer-to-peer lending and robo-advice.

Let's look at some facts from today's financial advisery industry

According to McKinsey's PriceMetrix annual report, one of the ways advisers have maintained revenue growth, is through an increased focus on new client relationships. In 2018, advisers opened 8.1 new client relationships, up from 7.6 in 2017. However, we all know every human has his or her limits, and advisers are no exception. One cannot manage more clients every year. Now imagine, if you had the tools that would enable you to gain and manage more clients every year, without putting in extra hours!? This is something only technology can do.

One more indicator shows us where new revenue growth is: revenues from fee accounts grew by 17% in 2018, according to the previous year, while revenues from transactional accounts declined by 5% year over year. It's clear, advisers need to focus on fee accounts. And the best way to do that is by leveraging technology to offer added value through subscription models.

Subscription is the new name of the game

Let's dig deeper into the data of revenue growth. We can see that it was further propelled by the fact that fee assets are more productive than transactional assets. So, clients are more and more willing to pay a fee that will secure them permanent help in managing their finances. And by permanent, they mean available 24/7 through a mobile app.

Fee-based revenue represents a record two-thirds of adviser revenue, and fee-based assets grew from representing 33% of all assets in 2015 to 47% of all adviser assets in 2018. It's a clear trend. Clients are welcoming fee-based methods, so adding a subscription fee for your advice to their account should be easier than you think.

Another report showed that 40% of financial advisers believe mobile apps, accompanied with digital platforms, will transform wealth management. In contrast, only 27% of advisers reported that 'robo' would be poised to transform the space within the next few years.

With the aim of becoming more effective at work, we started looking for a solution. As we didn't find one in the market, we decided to develop the MoneyRebel platform that provides the possibility to upgrade existing businesses. Today MoneyRebel is an all-in-one platform that offers a digital advisery experience that will help financial advisers introduce a subscription model and evolve their business, also with millennials in mind.

For further information contact **Jaka Kladnik**, **MoneyRebel COO – jaka@moneyrebel.com** or tel: **+386 41 200 003**.

Sources: McKinsey's PriceMetrix annual report; Accenture consulting report: Millennials and Money; CGI survey: Disruption in FinTech

Explaining gross roll-up as an offshore bond tax benefit

Rachael Griffin TEP FPFS, Head of Trusts & Technical Solutions at Old Mutual Wealth.

Offshore bond tax benefits can reap rewards for your clients and provide an opportunity for you to demonstrate the value of advice.

For those investors looking to move to the UK or for returning UK expats, an offshore bond could be an ideal investment wrapper. An offshore bond can offer access to a wide range of investments, consolidated administration including online portals, portability across jurisdictions, and UK tax benefits including Inheritance Tax planning solutions. In this article, I will look at some of the key benefits of offshore bonds for UK residents (including future residents).

Let's look at the key benefits of 'gross roll-up'. This term is often used, but what does this actually mean and does it really provide value for investors?

The concept of gross roll-up is a simple one - an investment can grow more efficiently because the income it derives isn't taxed at the point it is earned*, and the gains made by the assets within the investment are not taxable when the assets are sold within the investment 'wrapper'. The form of the 'wrapper' is often an offshore bond located in an offshore location like Ireland or the Isle of Man.

Conversely, directly held investments (such as equities, sovereign and corporate debt**, OEICs, property funds, and unit trusts) which can generate income in their own right are subject to immediate taxation in most countries where the investor resides. These investments may also be subject to taxation when they are sold, in a similar way to capital gains tax liability in the UK.

Key benefits of gross roll-up

- The offshore bond has the potential to grow faster than an investment that is taxed at source.
- Once inside the bond, investments are allowed to grow virtually tax free* until such time as a chargeable event occurs. This happens in situations such as the death of the last life assured, when partial withdrawals are taken which exceed the 5% tax-deferred allowance, or the maturity or full surrender of the bond.
- No limitations apply to the total amount that can be invested.

A case study example to show efficient growth

Let's look at a simple fictional case study to demonstrate the concept of gross roll-up over a ten year period. Here it is easy to see the value it could provide for an investor.

Neil, a 40 year old UK expatriate, is working in Cyprus on a short term contract. He invests €250,000 as a lump sum in an offshore bond and holds the investment over a ten year term. During that time there is 6%

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Easy access and the overlooked risk

Tavistock points out that recent news events have brought to light the risk of suspended funds and the distress these restrictions can cause for investors.

This news is bound to throw some shade on the investment industry, but what does Tavistock Wealth Limited (TWL) do to mitigate such situations?

We have been trading for five years, managing circa £1bn across our 9 UCITS funds and in that time, have instigated strategic partnerships with two of the world's biggest financial institutions; iShares by Blackrock, who's ETFs are predominately used in our funds and Morgan Stanley, who provide a protection level for our Protection Portfolios (funds). We typically invest in ETF's with high liquidity issued by the largest providers, meaning that if investors chose to withdraw, cash can be raised on any given trading day and provided to the investors account with their promised value. All of the funds are actively managed, allowing us to invest in multiple asset classes and be globally diversified. The same principles apply in our Protection Portfolios as detailed above, but with an added layer of protection from Morgan Stanley.

We appreciate that going global brings hand in hand another layer of risk; currency risk. Too often this risk is overlooked, but at TWL we mitigate this risk as much as possible by hedging the majority of overseas exposure back to the base investment currency.

So, where do we invest and how quickly can we redeem if needed?

- The way we invest money allows us to hold tens of thousands of underlying positions on a global basis across multiple regions/countries.
- This gives the portfolios high levels of liquidity and a well-diversified investment approach.
- What this means is we can access the market with a click of a button and we can disinvest just as quick.
- Investors are never locked in for a fixed term as our funds are daily dealing, UCITS compliant and invest in highly liquid assets.
- Most importantly this means we are able to sell out of our holdings when investors need to withdraw money.

How quickly can Investors access their money and are they locked in for a fixed term?

Investors are never locked in and there is no fixed term. Investors can access their money, invested in the fund, whenever they need it (ie trading days only) subject to the normal T+4 settlement cycle.

The Protection Portfolios lock-in the gains and limit the downside. This is ideal for cautious investors, people with a low capacity for loss, those at or near retirement, as well as those looking to protect the gains they have made.

Both Protection Portfolios are available via Novia Global. To find out more, please visit: **https://tavistockwealth.com/acumen-capital-protection-portfolio/**

For further information contact **Connor Stewart – connor.stewart@tavistockwealth.com** or tel:**+44 (0)1753 867 000**.

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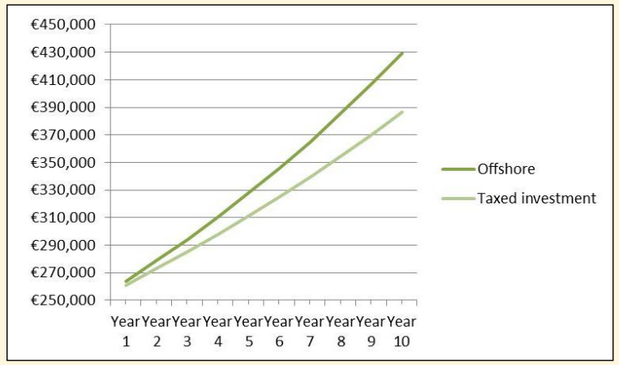
Explaining gross roll-up as an offshore bond tax benefit

growth on the underlying assets. If we assume 0.45% charges on the offshore bond per annum, net growth is 5.55%. With an assumption of 20% tax deduction per annum on the 'taxed investment' and a slightly lower annual charge of 0.35%, this provides a 4.45% net annual return.



The gross roll-up has provided an efficient environment for the investment to grow. The result is an investment value of €429,064 within the offshore bond versus €386,389 with the taxed investment after ten years.

This comparison only includes a single management charge of the product provider. There may be other costs to consider, including the facilitation of any advice/investment fees from the investment.

Managing the money out of the investment

Whilst gross roll-up provides a gross return above that of alternative taxed products, it is important to consider how best to manage the exit from the offshore bond. It can often undo the good work achieved within the bond if all the money is removed in one go, resulting in tax being assessed in a single tax year. Investors should consider the options for a staggered approach as well as who might be best to own the investment at the point of exit; for example owning the bond jointly with a spouse or transferring it to a spouse who pays a lower rate of tax could prove beneficial.

Demonstrate the value of your advice

The exit from the offshore bond is often the time when an informed adviser can demonstrate the value of their advice, protecting the gross investment gain achieved through gross roll-up.

Follow us on LinkedIn (**www.linkedin.com/company/oldmutualinternational**) for more updates on tax benefits of offshore bonds or visit our online technical centre, a hub of knowledge for you.
https://www.oldmutualinternational.com/Europe/Adviser/technical-centre/

For further information contact **David Matthews – david.matthews@ominternational.com** or tel: **+44 (0)1624 655 555**.

* *Except for any non-recoverable withholding taxes*
** *Equities, sovereign and corporate debt should not be held within the offshore bond when owned by a UK resident, in order to avoid an additional annual tax charge known as personal portfolio bond deemed gains*

Pension planning for peace of mind?

At GWMS we work closely with our business partners to offer intermediaries the very best solutions to protect and grow their client's wealth. With rapidly increasing life expectancy, this is particularly important in pension drawdown planning.

A strategy that aims to preserve a client's investment portfolio, despite drawdowns, gives them the best opportunity for long term security and enables the investors to pass assets to future generations.

With our partners at Levendi we are delighted to deliver this robust solution that meets these objectives for your clients. Freddie Flinn, Levendi Investment Management, details the strategy below.

The Levendi Thornbridge Defined Return Fund brings its 5% distribution share class to the offshore market.

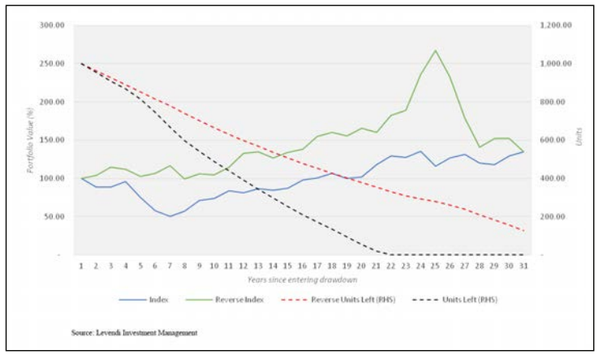
Increased pension flexibility, longevity and the reduction in annuity rates have combined to result in widespread demand for alternative income strategies that will provide higher yields for people in retirement.

Drawdown has become increasingly popular. Drawdown allows portions of a pension to be used to provide an income while the remainder stays invested. There are three main drawdown strategies;

- Redeem enough units to realise a fixed monetary value per period e.g. €3,500 per annum,
- Redeem a fixed number of units per period e.g. selling 2,000 units bi-annually or
- Redeem a fixed percentage of remaining units per period e.g. selling 1.25% of units left per quarter.

One of the key risks investors face when taking a fixed value from a portfolio is sequencing risk; this is the risk that markets fall initially only to recover later. The path of realised returns of an investor's portfolio is as important as the total return over the long term - short term negative returns can be very damaging.

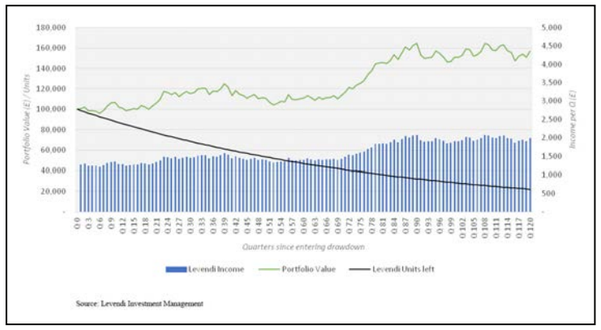
To illustrate this risk, we have created an index of returns and then created a reverse index which simply flips the order of annual returns on its head. It starts with the return from the last year of the initial index and works backwards. If the performance from year 29 to 30 was -12.03% in the initial index, the performance of the reverse index in its first year would be -12.03%. The performance of the index and the reverse index will be the same over the 30-year period, but the two indices take different routes.



In this example the investor takes £4,000 annually from a £100,000 portfolio. If the index takes the first path, the initial downturn in the index and subsequent decline from year four drastically affects the number of remaining units in the investor's portfolio. The low level of the index means that more units must be sold to meet the £4,000 requirement. The portfolio is unable to recover and runs out of units in year 22. If the index takes the second path, the increase in the level of the index in the early years means that fewer units must be sold and so the portfolio pays income for well beyond 30 years – this is sequencing risk in action.

One way to avoid sequencing risk is to redeem a fixed percentage of the remaining units. The Levendi Thornbridge Defined Return Fund (the Fund) offers a distribution share class that pays 1.25% per quarter. Not only is the annual distribution of 5% attractive but the Fund avoids sequencing risk and ensures that the number of units will never run out. Instead the number of remaining units will reduce proportionately over time at the same pace, regardless of market conditions. The caveat is that income will vary with the value of the Fund. To combat this, Levendi use a risk management process that aims to keep volatility between 5% - 7% (1 Year vol for the Fund is 5.31% at the time of writing).

In the second chart, the performance of the Fund has been simulated using 6% volatility, a realistic assumption. Over 30 years, based on this example, the capital value of the remaining units increases by roughly 60% and the investment has offered a quarterly income of



1.25% which has increased from about £1,250 to about £2,000. Over 500 simulations, the average income was £1,601 per quarter and the average final portfolio value was £156,861 (starting with £100,000).

If the Fund meets the return target, investors will receive a regular income that rises modestly over time and the value of the remaining units should remain stable. The Fund only has exposure to major equity market indices which tend to be less volatile than individual equities and the assets are very liquid, based on the liquidity of the underlying futures and options markets.

For more information on the distribution shares as part of a long-term drawdown solution please contact your GWMS Regional Sales Partner or call our **Head Office** on tel: **+44 (0)1525 861 983**.

It's about time in the markets, not timing the markets

A common mantra in investing circles is "it's about time in the markets, not timing the markets". In other words, the best way to make money is to stay invested for many years, rather than worrying about whether now is the best time to invest. In this article, Tilney Research Manager Tom White examines the case for staying invested over the long term.

What is timing the market?

It's natural to be concerned when markets fall – which is why some people try to time the market. This involves trying to second-guess the ups and downs, to buy when prices are low and sell when they are high. This is very difficult to do, and getting it wrong means locking in losses and missing out on gains.

Another example of timing the markets is sitting on the sidelines during periods of volatility and waiting for things to improve. This could be by selling all of your investments or holding back from investing new money. And with political issues such as Brexit and the US/China trade war causing stock market volatility throughout 2019, many people have been doing this recently.

Missing the best days

Not only is timing the market difficult to get right, it also poses the risk of missing the good days. Historically, many of the best days for the stock markets have occurred during periods of extreme volatility.

Anybody who pulls money out in the early stages of a volatile period could miss these days, as well as potentially locking in some losses. For instance, between May 2008 and February 2009 in the depths of the global financial crisis the MSCI World index dropped by -30.4%. By the end of 2009 it had bounced back +40.8%.

The risk of inflation

Inflation is another risk of keeping your money out of the stock market. Its power can be seen in the steady increase in the price of goods – from a first class stamp to a one-bedroom flat.

Money kept in cash won't keep pace with inflation. Your account balance won't decrease, but you'll lose money in 'real' terms (you'll lose spending power). Conversely, investing has the potential to outpace inflation and give you a 'real' return over the long term.

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It's about time in the markets, not timing the markets

The importance of time in the market

Instead of trying to time the market, we believe that spending time in the market is more likely to give you good returns over the long term. We base our investment decisions on the long-term fundamentals rather than short-term market noise.

Of course, this means experiencing the bad days as well as the good days, but markets and wider economies have a tendency to go up over time. For instance, the MSCI World index has delivered average annual returns of +10.9% since it was launched in 1969. We believe that successful investing requires patience and taking a long-term view, and being comfortable riding out the short-term ups and downs for the chance of better returns over longer periods of time.

The chance of losses reduces over long periods of time

You can see evidence of this trend by looking back at how the stock market has performed in the past. We calculated the minimum and maximum annualised returns that you could have received by investing in the global stock market for every single 1, 3, 5 or 10-year period since 1970*.

Returns from 1-year periods were extremely varied – ranging from -30.27% to 56.24%. This demonstrates the volatility that can be seen in stock markets over the short term. But over 10-year periods (such as from 1970 to 1980), annualised returns ranged from 0.21% to 23.69%. Not only were there no periods where the index fell, but the range of potential annual returns was also much narrower.

Although the past can't be taken as a reliable indicator of the future, this suggests that investing for the long term decreases the chance of overall losses. On top of this, it suggests that short-term stock market volatility tends to cancel itself out over longer periods of time.

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* *Based on the performance of the MSCI World index from 1970 to 2019, across calendar years, with annualised returns.*

Source for data: Lipper, July 2019.

Currency update

GBP

The Pound has been struggling over the last month after a slew of disappointing data. It wasn't all bad news, but the contradictions did nothing to assist Sterling. The construction PMI came in at 45.3 in July and services reached 51.4, above forecast and a point higher on the month. Retail sales were almost flat at 0.1% above the same month last year and the Halifax and the Royal Institute of Chartered Surveyors reported falling prices for UK residential property. Manufacturing output fell 0.2% in June and industrial production was down by 0.1% for annual declines of 1.4% and 0.6%. Britain's gross domestic product shrank by 0.2% in the second quarter of the year. Basic earnings were 3.9% higher but unemployment ticked up by 3.9%. The National Institute of Economic and Social Research said there is "a one-in-four chance that the economy is already in a technical recession". The Bank of England held interest rates and the quarterly inflation report gave an appropriate note of caution.

The key issue continues to be Brexit. While the new PM's decisiveness in appointing a new cabinet led to a brief surge for the Pound, the increasing likelihood of a no-deal departure is putting pressure on the Pound. Minister Michael Gove recently confirmed that he is "working on the assumption" of no deal and will head a special committee to plan for that outcome. Parliamentary recess may mean that the issue is on hold but the rhetoric continues to trouble the financial markets. Compared with its position prior to the referendum three years ago, it is 13% lower. Relative to its place in the immediate aftermath, it is down by 6%. The only piece of good news came from House of Commons speaker John Bercow, who insisted that he would fight to prevent a shutdown of Parliament by the Prime Minister. When asked by an audience member if Parliament could prevent a no-deal Brexit he said "Yes" but this was not enough to assist the Pound.

EUR

In Europe, the composite PMI was a three-month low at 51.5 and of greatest concern was the German manufacturing PMI which was the weakest in seven years at 43.1. There was better news with the German services PMI, which came in at 54.5. Confidence measures reflected the results. GfK and the European Commission showed falling confidence among German and Euroland consumers and across the business spectrum. Gross domestic product for the euro zone expanded by a provisional 0.2% in the second quarter, in line with forecasts but only half the growth achieved in Q1. Both German and pan-European inflation held steady at 1.7% and 1.1% respectively.

The reaction of the market is interesting; economic sentiment plunged in August, yet the Euro moved higher. The wider global picture and the current situation in Europe meant that pressure was lessened on the Euro. In Italy, the decision to call an early election due to problems with the coalition and the news was welcomed by the market. The European Central Bank kept monetary policy unchanged and hinted at easing in September. Despite Mario Draghi stating that the "outlook is getting worse and worse," the fact the Euro did not have to work hard to beat the retreating pound but did lose out against the US Dollar. It may be that the wider global picture will continue to influence the Euro while there is little to let it take control of its own destiny.

USD

The Federal Reserve had delivered the expected quarter-percentage-point rate cut after US inflation was up from 1.6% to 1.8%. There was little clarity from Chairman Jay Powell about whether it was a one-off move or the beginning of an easing programme. The strength of the US Dollar continues, largely unchallenged by the other major currencies. GDP growth slowed by less than expected in the second quarter. ADP reported 156k new jobs in July, supporting predictions that the latest employment report would show nonfarm payrolls increasing by 164k. The Dollar strengthened by 0.6% against the Euro and by 27% against the struggling Pound. Mostly the ecostats were supportive, although manufacturing PMI came in at 50.0, the lowest reading since 2009.

The US-China trade war continues to be a key issue and the US vacillates between stoking tensions with accusations of China being a currency manipulator from the US Treasury and easing them with a postponement of additional tariffs announced just a few weeks prior. The 10% import duties on Chinese goods from 1st September have now been postponed until 15th December. The change of heart came with an acknowledgement that the tariffs are driving up prices for US consumers. Investors are considering whether the tariffs will be implemented in December or whether it is a bargaining chip to put further pressure on China. In the meantime, the trade war continues to have an influence on global currency markets due to the impact on global trade.

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