

News & Views



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Hedging your bets

The thought of a fund that might deliver positive returns despite falling markets is very appealing, but is it actually possible? This is the potential being offered by 'absolute return' funds which reckon they can beat cash and smooth out market returns.

They use a variety of different techniques. One, the multi-asset strategy, blends asset classes like equities and bonds with alternatives such as hedge funds or gold. Therefore, when the mainstream asset classes are losing money, these managers have the opportunity to invest in alternatives delivering positive returns. The other main strategy uses 'hedging', ie: invest purely in equities, but 'short' some of those stocks. This involves borrowing them from someone else, selling them and then buying them back at a later date. There is a small price for borrowing but if the market moves down, the manager buys back the stock at a lower price than it was sold, making a profit in the turnover. This acts like an insurance policy, repaying some of the loss made on the fund holdings which will have fallen with the market over the same period.

Whichever approach is taken, the result should be smoother returns. However, neither should they be seen as a panacea. Diversity is a good thing but a manager still has to make choices – and can make the wrong ones. Shorting stock is a particular skill and could even increase losses. So, despite the label 'Absolute return', always remember that this is an objective only; there are no guarantees.



Beware of inflation

When buying an annuity, one issue you should always consider is the long-term effect of inflation. If the rate of inflation increases, the value of your income will fall because, as prices rise your money is able to buy less. One way to safeguard against this is to buy an index-linked annuity, which is linked to the Retail Price Index. By doing so, you ensure that, as inflation rises, so does your income. Similarly, escalating annuities, where your income increases each year at a rate set by you, also help combat the effects of inflation. However, do be aware these annuities start at a lower income level to balance out the expected growth in the future.

Welcome to the first edition of News & Views.

We've picked a few articles for you to look at - investment issues, low interest rates, annuities - I hope these articles are useful. Call if you need to know more - about anything!!

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The right cash ISA

Cash ISAs are some of the most straightforward investment products on the market and are designed to appeal to more risk-averse investors. For the 2009/10 tax year, the annual allowance is £3,600 (or, from October, £5,100 if you are aged over 50). The choice is wide, with some providers offering the flexibility of easy access (with perhaps lower interest rates) while others offer higher rates, particularly if you are prepared to tie up your money for longer. However, the headline rate is not everything. Short-term offers and bonus rates don't always last so you need to check if there is any guarantee that the rate will remain competitive should interest rates change.

The effect of interest rates

If interest rates change, one of the first concerns for many people is their mortgage interest payments on property investments. Most mortgage repayments tend to be variable, so the amount you pay fluctuates with changes in base rates.

The main reason for changes in interest rates is to control inflation. Mortgage repayments form part of inflation statistics and conditions in the housing market are a key consideration for the Bank of England when deciding interest rates. Rising interest rates can be used to help to cool demand if the market appears to be overheating as they deter people from moving by increasing the cost of mortgages.

If you believe interest rates are likely to rise (or simply like the certainty of knowing how much you'll be paying each month) a fixed rate mortgage may be most appropriate. Your repayments will be set for a certain period of time and are therefore not vulnerable to interest rate rises (although you will also not benefit from cuts). Another possibility is a capped rate mortgage, which means your rate will not increase above a specific level but you will receive any cuts. However, like fixed rate mortgages, most revert to the variable rate once the agreed period finishes.

As mortgages are held over long periods of time, even minor changes in repayments can add up to substantial sums over time. It is always worth discussing a possible new mortgage with your financial adviser when any discount or lock in periods end.

If you are a saver, rising rates mean higher income and you should make sure your bank is passing on all the benefit. Plenty do, so don't stick with one that doesn't. Cuts, however, mean less income as banks rarely hesitate in passing on lower interest rates to savers. It may therefore be worth keeping an eye on alternative deals to get a better return.

Interest rates also have an impact on those buying an annuity because you are locking into long-term income stream at current rates. Rises therefore are good news. Cuts, however, can be bad news as those income rates will also be cut. However, there are many options now available if your annuity purchase is linked to retirement. The best idea is to get expert advice and make sure you make the most of your money.



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