MI Financial Services
Newsletter Update
May 2010

A new political dawn

After a couple of nail-chewing weeks, the UK finally has a new Government and, while the Conservative-Lib Dem coalition may not be quite what investors would have wished for, then again, it is not as bad as they might have feared. But this is unchartered territory with the UK coping with an economic crisis and a political set-up not seen for a generation. Do investors need to prepare themselves for a bumpy ride? Or are the new government's policies likely to bring stability?

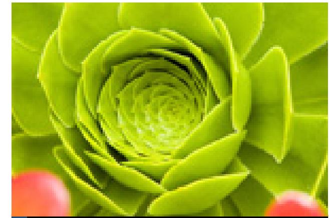
How is a hung parliament likely to affect markets?

First, it must be said that some measure of certainty is welcome. Markets hate uncertainty and the mere fact that a government has been formed has allowed them to concentrate on other areas (like the crisis in the Eurozone). The pound has seen a small rally against the Euro since the election, though this may be more a function of the potential weakness across Continental Europe than a vote of confidence in the new government.

More certainty of government is good for gilts, as is the fact that all the major rating agencies said that the outcome of the election had not changed their view on the outlook for the UK. That said, many other problems remain: Over-supply continues to be an issue and the rating agencies may not look so favourably if credible steps are not taking relatively quickly to deal with the deficit. All eyes will be on the new budget on 22nd June.

It is difficult to make a case for any rise in interest rates in the short term and most forecasters are predicting the smallest of hikes or none at all by the end of the year. With tax rises and public spending cuts on the horizon – plus deflationary pressures, such as unemployment, still at work and sterling stronger – any interest rate rise could be crippling for the recovery. The Bank of England has indicated rates are likely to remain low for longer than the market currently. However, that does mean income seekers will have to con-tinue to look for alternatives to cash.

For their part, equity markets have more to worry about than the UK election. They are, it seems, more concerned with global growth prospects and the eurozone crisis than they are with the domestic politics of the UK. With two-thirds of the FTSE 100 earnings coming from outside the UK, this is certainly a more appropriate focus. However, the June Budget may encourage a renewed focus on domestic issues.



Welcome to a post election update to the April edition of our newsletter.

We hope you find the contents of interest, and if you have any questions about any of the issues raised in this update or our April newsletter, please do not hesitate to contact us.

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Planning for success

Benjamin Franklin's belief that "by failing to prepare, you are preparing to fail" might be something of a cliché in the twenty-first century, but it is worth thinking about before you begin the financial planning process. Not only do you need to make your objectives clear, you can also make them SMART. This is business speak for making sure you are Specific about what you are trying to achieve, can Measure the success (or failure) to keep your plans on track, keep them both Attainable and Realistic given your own circumstances, and that in the end, you will see something Tangible in return for the work you have put in.

Specific policies of the new Government

As yet there is relatively little clarity on the policies from the new Government, which has simply made it clear that there is a very large hole in the nation's finances that it needs to take steps to address. That said, there are some clear areas of focus.

The first – and perhaps most noteworthy – is capital gains tax. With top rates of income tax now at 50%, the disparity with capital gains tax, which is currently charged at 18%, is all the more apparent. A rise in capital gains tax to 40% or 50% was a significant pillar of Liberal Democrat policy and the new administration has said it will seek "detailed agreement" on taxing "non-business capital gains at rates similar or close to those applied to income".

It is not yet clear whether the new rules will include the abolition of the annual allowance, whether they may reintroduce indexation or whether they will only apply to certain sorts of asset.

For the time being, plans for inheritance tax cuts have been set aside but the first Budget will see a significant increase in the personal allowance, to come into effect from April 2011. However, this is unlikely to reach the level of £10,000 set by the Liberal Democrats, which has been adopted as a "longer-term policy objective".

Pensions are unlikely to be left alone. Compulsory annuity purchase at 75 is set to go, which opens up some alternative income-generating options. The coalition has already stated it will restore the earnings link for the basic state pension from April 2011 with a guarantee that pensions will be raised by the higher of earnings, prices or 2.5%, as proposed by the Liberal Democrats. The retirement age is also likely to be raised.

Coalition is not a disaster. Markets had expected a hung parliament and the current compromise is probably as good as they could have hope for. The true extent of the compromise deal made by the Conservatives is unlikely to be seen until the Government's first Budget. This is very much a case of "watch this space".

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