CHAMPAIN
FINANCIAL SERVICES

Bawtry
Selsfield Road, Ardingly
Haywards Heath
West Sussex RH17 6TJ

01444 229 520
info@champain.co.uk
www.champain.co.uk

Technical Update No. 68 7th December 2020

Investor / Saver

The benefits of active funds:

When allocating funds in a portfolio, one of the questions investors face is whether to use active or passive funds. Simply put, active managers try to beat their benchmark. They will try to pick the best countries, sectors or stocks, and gather them up in a portfolio with the expectation that their return after fees will be above their benchmark index. Active fund managers claim they can beat the market, i.e. they can interpret information much better than other market participants and generate superior returns. While some can deliver stellar returns, the reality is that very few active managers can achieve exactly what they claim. That was the case in 2019 and will probably be the case this year too. Yet investors often pay a hefty price for active management. The reason for this underperformance is simple, according to the tenants of Efficient Market Hypothesis: investors compete to exploit with a profit any available information about earnings, macro and many other factors that affect the value of public companies. Stock prices adjust so quickly it is almost impossible to find mispriced stocks and exploit it for a profit. The problem with this theory is that it claims that those few who do indeed beat the market consistently are just riding on luck. If that's the case, does it make sense to pay an active manager and when? This is a prime time to employ the skill of an active manager. Technically this should be the case for any market, including in the US, despite its reputation of being one of the toughest markets to beat over the long run. The coronavirus crisis, and other episodes of market volatility - the fourth quarter of 2018, the Euro crisis in 2010-2012, the financial crisis of 2008, to name just a few - show that there are times when being active and daring to act and be contrarian can lead to outperformance.

Champain Financial Services Ltd. is a member of Best Practice IFA Group Limited, which is authorised and regulated by the Financial Conduct Authority.
Champain Financial Services Ltd. Registered in England No. 6800575. Registered Office: Palmerston House, 814 Brighton Road, Purley, Surrey, CR8 2BR.
Best Practice IFA Group Ltd. Registered in England No. 4490633. Registered Office: Broadlands Business Campus, Langhurstwood Road, Horsham, West Sussex, RH12 4QP

Property Owner

Brexit and house prices

On 31 December the post-Brexit transition period ends and, with or without a free trade deal with the European Union, the UK will start life outside the EU's single market and customs union. That will, pretty much all economists tell us, have a substantial economic impact on our lives. But what exactly will those impacts be – and how will ordinary people experience them? The Times describe how the two varieties of Brexit are likely to impact house prices and mortgages:

Deal:

Leaving the EU with a free trade deal would, according to the Treasury's independent Office for Budget Responsibility be a long-term drag on the economy, reducing economic output by around 4% relative to otherwise. But it would mean any short-term disruption, above and beyond the huge coronavirus impact, would be avoided. Leaving the EU with a successful trade deal probably won't have a short-term negative impact on house prices. In the longer term, the price of housing will be determined by the balance of supply of new housing and the demand for it and also interest rates. Moving from EU membership to a free-trade deal with the bloc is unlikely to directly influence these major structural determinants. As for mortgages, most borrowers' repayments are indirectly determined by the main national interest rate set by the Bank of England. Leaving the EU with a trade deal would be a more benign economic scenario from the point of view of the Bank's rate setting committee. It might bring forward the date at which the Bank raises rates, relative to a no-deal scenario on 31 December. And that could push up mortgage repayments for many households. Yet the Bank is mindful of the overall economy, which is still in the grip of the coronavirus emergency, and financial markets are not expecting significant rate rises from the Bank any time soon, whether there is a Brexit deal or not.

No deal

Some surveyors are nervous about the impact of a no-deal Brexit on the UK housing market. Several cite it, alongside the impact of Covid, in the latest survey by the Royal Institution of Chartered Surveyors (RICS) as a potential dampener on the market. If unemployment rises sharply next year because of the coronavirus crisis and a no-deal Brexit that's unlikely to be positive for house prices. Yet it's hard to say with any confidence that house prices would fall in the event of a no-deal Brexit, especially as they have held up extraordinarily well in the face of the coronavirus crisis, which has seen the biggest shock to the UK economy in some three hundred years. As for mortgages, financial markets are currently pricing in the Bank of England cutting interest rates below zero in the coming months to help support the economy. Many analysts think a no-deal Brexit could be the factor that pushes the Bank to take such a plunge into negative territory for the first time. While negative interest rates probably wouldn't result in a fall in average mortgage repayments from their current ultra-low levels, it would ensure they didn't rise. This could help cushion the financial blow of a no-deal Brexit for some households.

Property Owner

Will forced house sales pull prices down?

House prices were predicted to fall as soon as lockdown hit, but that hasn't really panned out. The stamp duty holiday is being cited as a potential reason, so it's definitely worth keeping an eye on prices when that ends. Commentators point out that we're seeing a lot of people who are reassessing where and how they live, with many looking to move away from busy city living into calmer, more rural settings. Time will tell, though, whether the trend continues. There's a lot to contend with in 2021 - before the stamp duty holiday ends there is also Brexit and the ongoing coronavirus pandemic to contend with. Now is, in some respects, an excellent time to buy as low fixed rate mortgages are rife and house prices are strong. August has, though, seen property values jump, according to David Price from 10ACIA Construction, in comparison to July - the largest rise since 2004 when prices increased by 2.7%. September saw another increase of 0.9%, which was 5% up on the same month last year which was the biggest yearly rise seen since 2016. We've seen the fastest growth in UK house prices in more than four years. Some experts still maintain that they are confident the market will be strong in 2021 meaning you shouldn't hold off on buying a house - but not everyone agrees. The majority expect house prices to fall. They already have slightly this past month and unless the SDLT holiday +/ furlough period are extended beyond March most would expect slightly larger falls each month, followed by a larger drop if other measures aren't introduced to fill the vacuum in April. There are still many businesses that will not be able to recover their losses, leading to increased unemployment. This is despite the surge in start-ups, no doubt aided by the furlough period and the previously unattainable free time that many of us found ourselves with earlier in the year. Sadly, though, the success statistics for start-ups are still as galling as they ever were, meaning that the majority will still fail within the first year. Hence, we cannot rely on this good-news-story to bridge the gap come April 2021.

Retired / Estate Planner

Inheritance tax bill warnings

The UK is in the midst of an economic crisis as a result of the coronavirus pandemic, putting the country in a double dip recession. The concerning state of the economy was once again highlighted recently as the national debt jumped to more than £2trillion. The budget deficit – the annual shortfall between spending and tax income – is expected to reach more than £400billion this year. This has led many to question how Chancellor Rishi Sunak will look to revive the economy, with many fearing imminent tax hikes. Mr Sunak has not yet revealed what tax policies he intends to change. A recent report published by the Office of Tax Simplification, commissioned by Mr Sunak, suggested rises in capital gains tax which could impact inheritance duties. But, as experts have highlighted, the number of families charged inheritance tax on gifts has climbed for three years in a row, and many are falling foul of the complex rules. Last week, the Office for Budget Responsibility projected that the number of estates subject to the duties will rise after the pandemic from 25,200 in 2019/20 to 30,400 in 2020/2021. Following a Freedom of Information request, HM Revenue & Customs this week revealed an increase in estates liable for IHT on gifts — up from 873 estates in 2015/16, to 920 in 2016/17 and 993 in 2017/18. The tax charged on gifts rose from £135m in 2015/16, to £156m in 2016/17 and £197m in 2017/18, the latest year for which data is available. Altogether, £5.2bn was raised in 2017/18 from 24,200 estates. Many families of older UK people who died from coronavirus could now face unexpected inheritance tax bills on their estates. Many of those who died unexpectedly will not have had time to plan their affairs. There are also the pitfalls of misunderstanding the rules. Many individuals who make gifts during their lifetime are unaware of the various available allowances and exemptions, let alone that their gifts could end up coming back to bite their beneficiaries in the form of a hefty tax bill. Mr Sunak has faced opposition from many within his own party over potential tax hike plans, many citing the plight faced by many self-employed workers who have been excluded from financial support during the Covid Crisis.

All

Business leaders warn of no-deal Brexit

Business leaders have warned that a Brexit "tidal wave" of red tape is going to hit British industry on 1 January even if a trade deal is struck in the coming days. The Confederation of British Industry deputy director general Josh Hardie pleaded with the UK and EU to redouble efforts to get businesses prepared, saying speed was now of the essence. He said he was confident there would be a trade deal in the coming days, because to walk the UK and 27 EU countries over a cliff edge on 1 January would be a failure of politics. As survey after survey shows businesses do not have the full information they need to be prepared for Brexit, Hardie urged the UK and EU to inform businesses what any trade deal would require them to do to be Brexit-compliant crossing from Dover to Calais, or any other UK-EU border. Business concerns come a week after a five-mile lorry queue developed on the approach road to the Eurotunnel in Folkestone as the French rehearsed Brexit checks. The CBI have called on the EU to state whether it will reciprocate on some of the "flexibility" being shown by the UK, which has decided to ease its Brexit customs and regulatory checks over six months to mitigate disruption. The CBI added that some critical information needed by business to prepare was outside the scope of the free trade agreement and needed to be agreed swiftly, including arrangements on cross-border data transfer, permits for business travel for engineers servicing machinery, and in particular rules of origin, which will determine what goods are defined as "British" and eligible for sale in the EU in a trade deal. Either way a cohesive and concerted government and business effort to mitigate the queues and chaos will be critical in the countdown to 1 January and in the immediate aftermath.

Property Owner

The stamp duty stampede – what next?

The UK's surging housing market could go into sharp reverse next year if the stamp duty holiday is not extended, risking a damaging slump, the government has been told. The £3.8bn stamp duty giveaway unveiled in July has been credited with fuelling a mini-boom in the property market, but it is due to finish on 31 March 2021 – the same date that the furlough programme and several financial support schemes are also scheduled to end. Experts believe ministers may be forced to extend the holiday to avoid a damaging downturn. Some believe that the end of the holiday in March will insert a cliff edge in demand at the exact moment we expect employment and incomes to be suffering most. If it is not extended, the argument goes, there is the risk that the surge in transactions and prices this year will be reversed in 2021. The stamp duty holiday means buyers of homes up to a value of £500,000 in England and Northern Ireland pay no stamp duty, with a reduced rate for homes above that. For someone buying a £500,000 property, the saving is worth £15,000. Previously the "nil rate band" for residential property purchases was £125,000. The warning coincided with government property market data that showed the number of stamp duty transactions in the third quarter was 68% higher than in the previous three months, and the amount of money raised from the tax was 27% higher. HM Revenue & Customs said this reflected the easing of the lockdown measures earlier this year and the introduction of the duty holiday. There have already been a number of warnings about what may happen when the stamp duty holiday ends, plus calls from various quarters for an extension. Some commentators have predicted that when the cut expires, transactions will fall almost as low as at the height of the first Covid-19 lockdown. Furthermore, the slump in demand is likely to coincide with a rise in forced sales as the ending of the furlough scheme brings a sharp rise in unemployment.

Investor / Saver

Will vaccines provide a market booster?

Pfizer and BioNTech announced that their coronavirus vaccine had been stunningly successful in trials. Moderna followed a week later, and then AstraZeneca and Oxford University. The stock market looks ahead and it’s not hard to see that a vaccinated world will improve the fortunes of beaten-down sectors. How much improvement, and how quickly? Answers are impossible, but stock market investors are clearly betting on normal life being restored at speed, at least at the level of individual companies. There’s even some talk of some “Roaring Twenties” years as consumers come out of hibernation. Stock markets are prone to wild swings – and one should note that EasyJet’s and Wetherspoon’s share prices, for example, are still about a third lower than they were on 1 January. But amid the din of conflicting signals, the rapid rebound thesis can’t be entirely dismissed. It could happen. Look at last week’s events in the retail industry. On one hand, the spectacular failures of Arcadia and Debenhams threaten 25,000 jobs. On the other, shoppers queued for hours to get into Primark stores and the big supermarket chains said trading had been excellent in recent weeks (one reason why they’re now returning their business rates relief). There is demand and cash out there. Add vaccines into the mix and it’s possible to imagine a mini-boom. There may still be 2.6 million unemployed in mid-2021 – as Rishi Sunak, the chancellor, warned in his spending review last month – but those who kept their jobs will be feeling financially safer than they have done in ages. Their debts will probably be lower because they didn’t have a summer holiday and lockdown was a frugal experience. House prices have not collapsed and interest rates look likely to stay low. Why not spend? You can see why share prices in consumer-facing companies are reacting.

Investor / Saver / Property Owner / Estate Planner / Business Owner

What next for Capital Gains Tax?

Alarm bells will be ringing for many taxpayers and their advisers following the report published by the Office of Tax Simplification (OTS) on 11 November 2020. Its recommendations, which are made independently to the Government, have the potential to increase capital gains tax (CGT) revenues by billions of pounds and could aid the Government in funding its response to the current pandemic. There is also a counter argument that a reduction in rates, whether temporary or permanent, could assist by providing an economic stimulus. There is real concern that the proposed changes, if brought into law, could lead to significant tax increases, both in terms of headline rates and also in terms of reliefs available. This may result in changes to investment behaviour as well as changes to the structuring of family businesses and in wealth planning generally. The OTS has suggested that:

- CGT rates should be more closely aligned with the higher rates of income tax so that the tax system is more 'neutral'. The report anticipates that doing this could result in an additional £14 billion of tax revenue per year. This assumes that taxpayers carry on as before and that no other changes are made to soften the effect that the increased rates would have; and
- The annual exempt amount (AEA) be reduced from £12,300 to £5,000. This would bring more individuals within the CGT tax net but could also deter affected taxpayers from realising similar levels of gain. In order to make tax compliance easier for affected taxpayers, the OTS has recommended that investment managers be required to report CGT information to taxpayers and to HMRC.

This is the first report from the OTS as part of a two-stage review of the UK's CGT regime. A second report, which is expected in early 2021, will explore technical and administrative issues in greater detail once the OTS has considered the responses to its second call for evidence. Given the content of the first report, the second report is likely to receive a lot of attention.

Past performance is not a guarantee to future performance. You may get back less than invested.
Thresholds, percentage rates and tax legislation may change in subsequent Finance Acts and reliefs from taxation are subject to change. The FCA does not regulate tax advice.

The content of this newsletter is for information only. It does not represent personal advice or a personal recommendation and should not be interpreted as such. Please do not act upon any part of it without first having consulted an Independent Financial Adviser.

For information about our services please contact Champain or view online.

END