What the Papers Say

This is the latest in a regular series of summaries where we look to review some of the main articles written in the financial sections of the Sunday papers.

These articles often cover issues that are important to our personal financial well-being and we hope that the summaries will provide you with information and ideas that will be of interest to you.

If you would like to discuss any of the issues raised within these summaries or any other financial planning issue, please do contact our wealth management division on 01204 414243.

"Quitting work is a cherished dream of millions"

The Telegraph

Many dream of retiring early, but how realistic is it and what sacrifices would need to be made to make it a reality? The Telegraph used an example of a 38 year old earning £43,000 per annum with existing savings of £30,000. The normal State Pension Age for a 38 year old today is age 67 and therefore able to access their pension at 57 at the earliest.

In the example, the 38 year old is targeting an income of two thirds of the salary (i.e. £28,000) in today's terms. A final savings pot of £700,000 would be needed in order to draw a 4% income throughout retirement at age 67. This increases to £933,333 at age 57 with a sustainable income of 3% throughout retirement. .

The following assumptions were made:

- Income at 4% could be taken at age 67 – this is described as the safe withdrawal rate.
- This is reduced to 3% at age 57 given the longer term over which the accumulated fund needs to last.
- The existing savings pot grows by 4.5% per annum up to age 67 which is deemed an achievable rate of return for a medium risk investor.
- A return of 6% would be needed to retire at age 57, which results in an increase the level of risk needed to generate the required returns.
- The £30,000 savings pot would have grown to £110,360 at age 67, but only £93,536 at age 57. As a result there would be a shortfall of £589,640 or £839,797 which would need to be made up through regular investment.

In terms of the additional contribution needed to retire early, this increases from £613 to £1,982 per month in the above example. The contribution can be split between pensions which would benefit from tax relief, together with investments into ISAs which could bridge the gap and provide a fund which could be accessed prior to retirement if needed.

In any event, this level of disciplined saving would leave the 38 year old with around £1,400 per month to live on, after tax!

"Employers will need to contribute a minimum of 8% to their workers' pension funds by 2018"

The Sunday Times

Currently the amount of money an individual, employer and the government must pay into pensions through Auto Enrolment is relatively low at 2%. It will eventually reach 8% by 2018 (4% employee, 3% employer and 1% tax relief). Many pension experts believe that 8% is a start but is still too low. Steve Webb the former pensions minister has previously stated that people generally "just budget what is the in the right hand corner of the payslip" and if a pension contribution has already been deducted it would not be missed. How accurate a reflection this is, is unknown!

The advantage of auto enrolment and the link to salary, is that as salaries increase so too will the pension contribution. This "default automatic escalator" takes away the need for individuals to increase their contributions as their income increases. Furthermore, contributions are boosted by tax relief, will hopefully benefit from capital growth and dividends, and perhaps more importantly the new flexibilities will mean greater access in retirement.

More chaos in the markets as Fed set to raise rates
The Mail on Sunday

On Thursday the US Federal Open Market Committee will say if is putting up interest rates for the first time since 2006. Analysts expect an increase of up to 0.25%, although some now believe that given the volatility in August the Federal Reserve will hold off until the end of the year. In the UK interest rates were maintained at 0.50% last week.

Very low levels of inflation together with falling commodity prices and a strengthening dollar and pound have driven down costs of goods in both the US and the UK. Figures due on Tuesday are pointing towards the UK falling back into deflation. It is expected that the UK will hold off raising rates until after the Federal Reserve. Vicky Redwood, the chief UK economist at Capital Economics said "We expect rates in the US to end 2017 at 3.5% compared with just 1.5% in the UK".

The FTSE 100 rose 75 points ending the week at 6,118. Over the year it is down 10% (6.1% with dividends) and up 5.6% over 3 years (18.5% with dividends). Over 5 and 10 years the index is up 11.2% and 14.2% respectively (34% and 65.5% with dividends respectively).

"Time to look to companies that pass the test of dividend cover"
The Telegraph

According to the Telegraph, UK investors are facing the biggest threat to their income in 30 years as falling profits have hit dividends. Last week Glencore axed its dividend following Tesco, Centrica, Severn Trent, Tullow Oil and Morrisons.

With interest rates being so low, investors are attracted to dividends and usually it is the larger companies that are more sustainable with attractive dividends. The FTSE 100 is heavily weighted to the resources sector where profits have collapsed during the past 18 months. The mining sector in particular has seen falling dividends at Rio Tinto, BHP Billiton and Anglo American.

Dividend cover is one of the easiest ways to check whether a dividend is vulnerable. The cover shows the degree to which a company's reported profits are greater than the dividend. For example, if the company's annual dividend is 5p per share and it generates 10p per share, it is said to have dividend cover two times. The closer to one the greater the risk.

In the FTSE 100, companies such as GlaxoSmithKline (0.8), HSBC (1.6), Royal Dutch Shell (1.06), BP (0.9) and Vodafone (0.5) have been amongst the most popular dividend stocks. But as shown by the dividend cover in brackets all are increasingly at risk as they fall closer to 1.

Higher dividend cover is not a guarantee of future payments, but does strengthen the ability of making payments to investors. Questor highlights BT, Sky and WPP as paying well covered dividends, plus insurance companies Aviva, Prudential and Admiral. Housebuilders have also revert to returning more cash to investors including Persimmon, Barrett and Berkeley.

As with all investments it is important to note that the value of investments and any income taken from them can fall as well as rise. You may not get back the full amount of your original investment.

Any questions?

If you have any questions on any of the articles covered in this publication or would like our help with any financial planning issue, please contact:

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