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Little sign of austerity in Budget

Most of the key changes announced in Chancellor George Osborne's Budget had already been leaked to, or guessed by, the financial press. There had also been plenty of heated political discussion in the days before he addressed the Commons. Although he had little wriggle room, given the scale of the deficit and the need to reassure ratings agencies, strong expectations of lower income tax bills for millions proved to have been well founded.

The Chancellor's major announcements on income tax reflected a trade-off between the Coalition partners. He announced that the 50% income tax rate above £150,000 would be cut to 45% from April 2013, with little loss in revenue according to his figures. He also unveiled a record increase in personal allowance of £1,100, from £8,105 to £9,205 in April 2013, with a target of £10,000 in sight. This news was soured somewhat by the decision to phase out age-related allowances as well as linking long-term State Pension Age rises to life expectancy.

Tax cuts for companies too

A number of changes with implications for corporate sector prospects emerged, including acceleration of the annual reductions in the main rate of corporation tax. This will drop to 24% this April, not the previously announced 25%, and then by another 1% in each of the following two years, to reach 22% in 2014 and perhaps later match the current smaller profits rate of 20%.

The personal and corporate tax cutting seemed at odds with the Chancellor's earlier austerity warnings and famous 'we're all in this together' catchphrase. Their affordability must depend heavily upon the accuracy of updated forecasts from the Office for Budget Responsibility, referred to in the Budget speech. These predicted an upward trend in UK economic growth (hitting 3% in 2015), a fall in CPI inflation to near its 2% target and a big drop in unemployment from an 8.7% peak. The Government seemed confident in contemplating the issue of very long-dated, or even perpetual, gilts.

Some Budget measures could hit wealthy individuals in particular. The widely-anticipated 'mansion taxes' were announced, including 7% stamp duty on properties bought for more than £2m, with a penal rate for purchases via offshore companies. The Chancellor also announced a clampdown on repeated exploitation of tax reliefs that currently have no ceiling; these will be capped at 25% of income. Such measures will be supported by general anti-avoidance rules due to take effect next year.

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Something less ordinary - when higher risk appeals

It is a fact of investment life that all stock exchange investments carry some degree of risk; many individual investors wisely adopt a strategy that avoids extremes of risk and also spreads exposure across a chosen range of market sectors or countries. Such a strategy, properly managed and maintained, moderates the risk of major loss whilst aiming to achieve the client's expected level of return on their investments.

Some people like to take a little extra risk

For more experienced investors, who have built a well-balanced portfolio of relatively cautious equity investments, there may be grounds for allocating a modest proportion of net wealth to investments with a more adventurous risk profile. It is something to discuss with your adviser, because any such strategy must be squared with your overall investment objectives and attitude to risk.

There are a number of interesting sectors to consider and fund managers that provide the means through which to invest. Higher risk investors will often be on the lookout for a new market or a sector with long-term potential and must be seasoned enough to deal with short-term losses. These new sectors could attract high returns, but there may be times when they perform less well than more staid investments. High risk does not guarantee high reward; it just offers the possibility.

Out of Africa

Volatility, financial or otherwise, means added risk and this can also be seen in areas of the world where there is less political stability and where there is ongoing political instability. Yet such areas, often with untapped natural resources and energetic local workforces, can create opportunities for growth. This is very much the case in parts of Africa.

This vast and varied continent could be worth consideration for those who already have exposure to the emerging economies of China and India or simply want to tap into a relatively untested market. Nigeria, a significant oil producer, and Kenya are among the countries in specialist fund managers' sights. South Africa, less in the news since the 2010 World Cup, has a well-established track record thanks to valuable deposits of gold, diamonds and industrial minerals.

Latin America is also interesting – Brazilian President Dilma Rousseff has claimed her country's burgeoning economy could grow by 4 per cent in 2012. Likewise, for investors wanting to keep closer to home, Eastern Europe has a number of exciting emerging economies and it has been mooted that Turkey, with one foot in Europe and the other in Asia, may beat its 4 per cent economic growth target.

Except when disasters occur, the oil and gas majors are usually solid earnings generators but the wider energy sector is always going to be hugely topical. It can have some big swings, such as the impact on power generator Tepco of the 2011 Japanese tsunami. There has been fresh interest in the renewables market and, although performance may often be dependent upon political decisions, areas like solar panels and wind turbines have emerged as important.

Shares that could recover

For some investors, there's enough excitement available within our shores and one option is to buy into a 'recovery' fund, where the companies in the portfolio will have been selected because they have been through some difficult times but are now believed by the fund's managers to be on the up again. Property is another sector with recovery potential – once seen as the road to riches, it now has less allure.

Funds focused on the commodities markets could also be worth closer examination. Likewise, there are funds that specialise in very small firms, such as in the biotech sector – some will fail and some will make it big, with the prospect of reward for the investor holding a diverse spread. As investment in the technology sector has shown in the past, having lots of investors pile in does not provide any guarantees; the greater the risk of individual failure, the greater the benefit of a well-chosen selection. Never keep such fragile eggs all in one basket.

Final salary pensions – facing up to the point of no return

In January it was announced that the last FTSE 100 company would stop its final salary pension scheme. Employees working for oil group Shell were told that, for new joiners, the final salary scheme will be closed from 2013 and instead they will be offered a new defined-contribution pension. Shell said it was taking the step to "reflect market trends in the UK" and the plan would be designed to ensure that the reward package in the UK for new hires remained strongly competitive.

There are still other employers, including non-UK-listed firms that do offer final salary plans, such as BMW, but they are now the exception rather than the norm, which has resulted in many people having concerns that their retirements are not going to be as comfortable as they hoped.

Final salary schemes are being left behind

With these pensions, workers accrue a chunk of pension entitlement for every year they work at a particular company. This is typically the equivalent of 1/60th of their salary when they leave the company or retire. Someone in such a scheme who worked for 40 years would get a pension entitlement of 40/60ths, two-thirds, of their final salary.

However, the demise of final salary pensions is linked to the fact they simply cost employers too much. A range of factors, including longer life expectancy, low inflation, weaker stock markets and increased regulation, mean these schemes place a massive cost and administration burden on the companies that offer them.

A reason for protest

Some private sector firms have even been threatened with industrial unrest if a final salary scheme is withdrawn. This also happened recently in the public sector, when thousands of workers took to the streets last June to complain about planned pensions changes.

As alternatives in the run-up to pension auto-enrolment, most organisations are in the process of moving to a defined contribution scheme, to which employees pay in part of their salary each month and the employer makes a contribution on top.

This places a greater burden on employees to save for their retirement. Another option is to offer a defined benefit pension scheme based on their "career average" salary rather than salary at the time of retirement – an option mooted for the public sector.

Facing up to reducing rewards

Career average revalued earnings offer retirees an average salary income in retirement as opposed to a final salary. This can be better than a money purchase scheme as the income is guaranteed, but less rewarding than a final salary pension scheme.

Those few firms who still offer final salary pensions may find it is worth doing so as it helps them recruit and retain their most valuable people. Experts say a pension is unlikely to be the main reason someone chooses a job, but if they have two offers on the table it could be a key reason to select one over the other.

Pension planning has never been simple, your financial adviser can help you make the best plans for your retirement.

Is a Sipp your cup of tea?

One of the notable features of the pensions market in recent years has been the rise of the Self Invested Personal Pension (Sipp), a tax wrapper, which can have considerable appeal through offering more choice, but also needs careful consideration before setting up.

The Financial Services Authority began regulating Sipp providers in 2007 and, for consistency with personal pensions and to aid comparisons, now proposes increased disclosure provisions. These would require providers to supply illustrations and projections for investments held within a Sipp and disclose any bank interest or commission retained on members' funds.

Scope for greater flexibility

All this suggests that anyone considering a Sipp does need to look carefully at the potential returns and the costs, and this is where the role of your adviser can be essential. However, these are the fastest growing retirement vehicles in the market place and are becoming a mainstream product in UK investment planning. With the final salary sector in terminal decline, many higher net worth individuals are looking for greater flexibility and the potential for higher returns.

A Sipp might be your cup of tea

The key Sipp advantage is wider investment choice compared to personal pensions. Money can be held in such investments as corporate bonds, commercial property (including Real Estate Investment Trusts), the AIM market and other UK and overseas equities.

For those who have worked for a number of employers and have pension pots tied up in other schemes, a Sipp provides a base for consolidation. Bringing these pots altogether may reduce fees and give access to better investment performance.

The prospective pension income for people in final salary schemes is such that they are in many cases unlikely to see transfer into a Sipp as offering a clear-cut advantage. But, a money purchase pot could be a more likely transfer candidate. And, before any transfer of an existing pension, checks should be made as to what may be given up from an existing pension arrangement – such as a guaranteed income at retirement, contributions from your employer and salary-linked pension income. The costs of moving pensions, which could include a transfer penalty from your current pension provider, must also be considered. An adviser's guidance should always be sought in these areas.

Meanwhile, a Sipp can also be used to house any accumulated additional voluntary contributions (AVCs) as well as 'Protected Rights' held in a separate fund by those who contracted out of the State Earnings Related Pension Scheme (SERPS) or State Second Pension (S2P).

Advantages of scale

Picking the right Sipp provider is important. Charges can vary considerably, depending on the type of Sipp held, the investments selected and the level of trading. But, generally, the bigger the amount to be invested, the more affordable the fees, and these should also incorporate set up, fund, trustee, administrative and consultancy charges. A big pension pot will also be better able to absorb the transaction fees of an active investor.

Pension planning is a long-term and complex process. And, unless you are comfortable monitoring funds and making regular investment decisions, you will find it easier if your financial adviser takes on much of the work.

News in brief (data compiled by The Financial Marketing Department except where otherwise stated)

There were signs of increased property market activity in January and February, partly attributed to the approaching 24th March end to the stamp duty holiday for first-time buyers at prices up to £250,000. In mid-March, the Government unveiled a scheme to facilitate 95% mortgages for suitable buyers of brand new properties.

Office for Budget Responsibility forecasts suggest inflation will continue to fall and settle near the official CPI target of 2%, but there remain concerns that rising oil prices could intervene. Supply uncertainties over geopolitical problems in the Middle East could hit UK pump prices, which topped 140p per litre for unleaded in late March.

Unemployment, particularly among the under-24s, continues to cause concern, but official Budget forecasts predict that the rate will peak this year at 8.7% and start falling. Government support for more apprenticeships and start-ups as well as accelerated reductions in the main corporation tax rate are expected to help job creation.

Late March saw a backlash from pensioners angry over the Chancellor's plan to phase out age-related income tax allowances. These will be frozen at 2012-13 levels, with no further rises until the basic personal allowance overtakes them. Automatic increases in State Pension Age based on life expectancy may adversely affect future pensioners.

Are you sitting comfortably?

Many families that have been feeling 'comfortably off' for the past couple of generations are in 2012 feeling rather less comfortable. The rest probably should be. They would have good reason. On top of the impact the credit crunch and recession have had on virtually everyone, the financial fabric of middle-class family life seems to be under threat. Many things once taken for granted are disappearing or diminishing.

The 40-year career, the final salary pension, the thriving family business (perhaps in retail) – all underpinning financial security – no longer provide such solid reassurance. Loss of a crucial income source is a major worry now that white-collar unemployment for forty-somethings is not unusual, and there are plenty of other pressures tending to erode family finances.

Despite the Budget concession, child benefit will be reduced or withdrawn from many middle-income families (more of which will soon be higher rate taxpayers) and, looking ahead, everyone will have to wait longer for their State Pension. Meanwhile, the inflation of the past two or three years will still affect future prices even if the annual rate does fall back to the 2% target. Low interest rates on some savings have also taken their toll.

Even tougher for offspring

One pleasure long enjoyed by the comfortably off has been the ability to help upcoming generations of the family at crucial stages in their lives. School fees have seen large increases over the past couple of decades and now, of course, there is the issue of university tuition fees and other costs associated with higher education. Many parents assist with the latter to spare their offspring the burden of student debt.

The other big issue for upcoming generations is housing. Finding an adequate deposit without a parental contribution, or timely inheritance, may be beyond even graduates able to secure a good job despite the disturbing levels of youth unemployment. Yet parents must have regard for the rising cost of everyday living, of residential care and even of dying, so may hesitate to hand wealth down when it could be most helpful.

We are financial advisers, not prophets of doom, so we see the adversity faced by many middle-class families as a challenge, not a disaster. Thoughtful financial planning can mitigate many of the threats to financial security at the same time as helping to strike a balance between spending on quality of life now and investing intelligently both for retirement and for the benefit of upcoming generations.

A little less comfortable

It is important to take professional advice before making any decision relating to your personal finances. This publication represents our understanding of law and HM Revenue and Customs practice as at the date of publication. It does not provide individual tailored investment advice and is for guidance only. Some rules may vary in different parts of the UK, please ask for details. We cannot assume legal liability for any errors or omissions it might contain. Levels and bases of, and reliefs from taxation are those currently applying or proposed and are subject to change; their value depends on the individual circumstances of the investor.

The value of investments can go down as well as up and you may not get back the full amount you invested. The past is not a guide to future performance and past performance may not necessarily be repeated. If you withdraw from an investment in the early years, you may not get back the full amount you invested. Changes in the rates of exchange may have an adverse effect on the value or price of an investment in sterling terms if it is denominated in a foreign currency.