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WEALTH

Get in shape for summer

Bank of England interest rates are now at the lowest level in 300 years, because of this, many investors now have to search far and wide to find other sources of income.

Play it safe

Standard savings accounts are the default option for many people. However, interest rates are generally not high on these. After tax (and with inflation), money saved in these can lose value in real terms. Luckily, there are alternatives, but people should look around carefully.

For new investors, the market falls over the past two years may be good news, bizarre as it may seem. Bond yields generally rise when interest rates fall and generally fall when interest rates rise. Hence, in this low-interest environment, share and bond values have dropped, but most companies are still paying out share dividends and yields on their corporate bonds (their long term IOUs).

The falls in value also mean that, for some investors, returns are up significantly. For example, a share that costs £1 and pays an annual dividend of 10p has a yield of 10% (10p/100p). If the share price drops by half to just 50p and the dividend remains the same, the yield doubles to 20% for new buyers. With markets in turmoil, good companies with high credit ratings were hit just as hard as those with a less impressive rating. Existing bond holders saw their initial investment values fall, although their fixed-income payouts were relatively stable.

Think as a fund manager

Fund managers will pick a diversified portfolio of income-bearing equities and bonds, or construct a fixed-income fund of various bonds issued by

different companies, with varying yields and maturity dates.

Many investors had relied too heavily on financial services dividends and bond issues to provide as much as a third of their income, which led to pain last year. The financial sector was the hardest hit. Those banks that have been nationalised or needed Government help could spend years paying back their State loans, leaving little to pay out to shareholders.

For new investors, the market falls are like a “buy-one-get-one-free” offer at the supermarket, but they should be careful to buy the right bonds or shares, or funds that invest into these. Some managers have described the current prices of second-hand bonds as a “once-in-a-lifetime” opportunity. With prices down, some corporate bonds are yielding up to 7% and even more for some companies, although the value of bonds, like any investment, can fall as well as rise and investors may not get back the full amount invested.

Most managers are playing it safe. A high yield means prices have dropped significantly. It could also indicate that investors expect a company to default; chasing high yields may cost dear in the end. Managers are moving into defensive stocks: the gas, water, electric and food companies. Their robust regular revenue translates into bond coupon payments and dividend payouts.

Income to consider

Equities and equity income bonds that offer quarterly, half-yearly or monthly dividend yields can boost your regular income. Bonds, either corporate issues from companies or government issues (gilts) can prove to be a significant source of fixed income. Remember, only consider investing in equities or bonds if you can afford to take a risk with your capital and can invest for the medium-to-long-term, this is at least five years. Fixed rate, regular savings accounts and Cash ISAs all help boost income on cash. Ask your financial adviser for some information on how you can augment your income.

Levels and bases of, and reliefs from, taxation are subject to change.

The value of your investment and the income from it can go down as well as up and you may not get back a significant proportion of your investment. Past performance is not an indication of future performance. Please contact us for further information or if you are in any doubt as to the suitability of an investment.

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