Teachers Financial Planning

Savings and ISAs

A guide to starting saving and some of the products available.

Saving is a lot like exercise, we could all probably do with a bit more but sometimes it can be difficult to motivate yourself to actually do it.

A common reason many people give for not saving enough, or at all, is that they don't have a sensible savings strategy.

Another reason is that there can appear to be such a vast range of options available that people don't know which is best for them.

Your savings strategy

A savings strategy is built upon the answers to the following questions:

- Why are you saving?
- Are your saving goals long-term or short-term?
- Are you prepared to risk your savings in investments for potentially higher returns or do you want low risk and lower interest rates?
- How will your tax position affect your savings?
- Will you need to access your savings quickly?

Once these questions have been answered it will be easier to work out a sensible strategy with achievable goals.

Creating a plan

First, create a document detailing all monthly income and expenditure. This should include one-off large payments which can be divided across 12 months.

This document should indicate what money remains after all of your regular payments and whether there is anything that can be saved on monthly outgoings.

Next, bearing in mind the amount of money available to save, set goals such as saving a minimum of £100 per month.

Risk and interest

Investing in the stock market is a potential strategy to try and secure a higher return on the money invested. However, investing carries increased risk and there is no guarantee that your investment will increase and it may go down over time.

Putting your money in a savings account or cash ISA is lower risk but the returns are likely to be lower.

The effect of inflation on savings

Inflation has a marked effect on savings. If the rate of inflation is high and an individual's savings are in a low interest account then the net result could be that the buying power of their savings is lower (the value is lower relative to prices).

A simple rule of thumb with reference to inflation and savings is that your money will still grow if it earns interest, but its buying power/relative value will only grow as well if the interest rate (net of any taxes) is higher than inflation.

We can advise you on creating a savings strategy.

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Personal savings allowance

Anyone starting to save should also be aware of their personal savings allowance. At present anyone paying the basic rate of tax (20%) can earn up to £1,000 per year tax-free from interest on savings.

Savers paying the higher tax rate (40%) can earn up to £500 per year from interest on savings. There is no savings allowance for savers paying the highest tax rate of 45%.

Interest earned on tax-free accounts such as ISAs or Premium Bond wins does not count towards the personal savings allowance.

ISAs

An ISA is a tax-free account for individuals to use for their savings or investments. There are a range of ISAs available to savers and this is where some confusion can arise.

You can save up to £15,240 into an ISA in 2016/17. The annual saving limit is due to increase to £20,000 a year in 2017/18.

ISAs can take the form of cash ISAs or stocks and shares ISAs which can be higher risk depending upon the type of investments you hold in them.

Cash ISAs can be fixed rate or easy access, and it should be noted that fixed rate ISAs will have a better interest rate than easy access ISAs.

There is also a Help to Buy ISA aimed at first time buyers and an Innovative Finance ISA which offers up to 6% interest but is more complex than an ordinary ISA.

The Innovative Finance ISA is based on peer to peer lending, whereby individual investors lend out their money to other individuals or businesses. Innovative Finance ISAs are higher risk in that if a borrower cannot return the lender's money, the money is lost. Additionally the lender's money is not protected by the Financial Services Compensation Scheme.

Lifetime ISA

The new Lifetime ISA (LISA), which will be available from April 2017, is designed to help people save for the purchase of their first home or for their retirement.

The LISA works in the following way:

- you must be aged between 18-40 years old to apply for a LISA
- individuals can save up to £4,000 per year in the LISA (as part of the overall £20,000 annual ISA contribution limit) and the government will add a 25% bonus to this sum
- people can contribute and receive the bonus until they are 50
- the maximum bonus payable is £32,000.

The money must be used for a first home (on properties with a value of up to £450,000) or towards retirement (where it can be taken tax-free after the saver's 60th birthday). Individuals may have a LISA and a Help to Buy ISA and money can be transferred between the 2. There are 2 options: a cash LISA and an investment LISA, and the savings or investment growth is tax-free.

Early withdrawals will lose the bonus, and interest or growth on the bonus. There will also be a 5% charge.

Talk to a member of our team about the Lifetime ISA.

Other savings options

Another straightforward option for saving is a savings account with a bank or building society. However, it should be noted that some current accounts have 'in credit' interest rates which are higher than savings account interest rates.

It might take a little research to find these accounts but it would be beneficial to anyone looking to save using a bank account.

Easy access savings accounts have a lower interest rate but the money can be accessed instantly. These interest rates do fluctuate so it is advisable to monitor them and switch accounts if need be.

Savings accounts include fixed rate accounts which also require the saver to leave the money in the account for a set time period. Although they do frequently offer a higher interest rate to savers compared to easy access accounts.

Premium Bonds are a secure way of saving; they are no risk as they do not pay any interest. The prizes represent an annual interest rate, but only for winners and the prizes themselves are tax-free.

Contact us for more information on savings.