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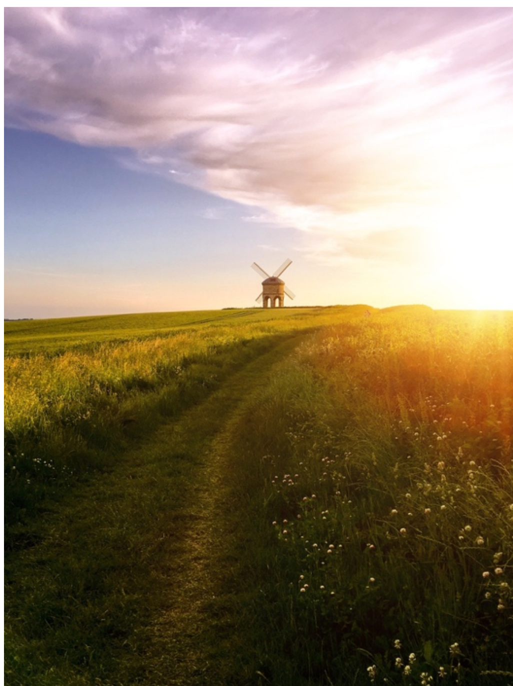
SOLUTIONS

Tel: 01926 400441
Email
info@warwickfs.co.uk
www.warwickfs.co.uk

# Savings and Investments

So much choice. Which is right for you?



**Why are we encouraged to save money?**

From childhood most of us are told to put away money to save for the future - perhaps for something special? Or perhaps to be sure that when we really need something, we have the funds to that we need, without taking on debt? Whether you place your money in a piggy bank, or in a multinational investment house, our aims are broadly the same; to provide for our future needs, and to protect ourselves against unexpected causes of expenditure.

When planning your finances, it is important to distinguish the difference between savings and investments. Savings are generally funds that you set aside but can be accessed relatively quickly. These savings are often for a specific short-term need or purchase, like a holiday or a new car in the next year or two. The most common way of 'saving' is into a bank account eg deposit account, where the money can be accessed in an emergency, and for every £1 you put in, you will get that £1 back and possibly with some interest.

Investments are designed to be held for a longer term, usually at least 5 years. You need to be comfortable with tying up your money for a period of time and should not consider investments unless you have some savings in place. Most investments are not guaranteed to return your money in full, although do offer the prospect of potentially higher returns than deposit accounts. Returns, risk and volatility are the factors that will determine a suitable place for your savings.

Savings and investment products range from a simple current account, which allows a small amount of interest, but facilitates regular payments and withdrawals without detriment to your savings. At the opposite end of the scale would be company shares, where you invest money in a company, with the prospect that the company will prosper and that the shares will increase in value over time. Whilst the benefits are potentially high, the risks are also much greater.

## Investment Options

**There are so many different mediums in which to invest, and here we look at just a few key areas:**

**Bank Accounts** – current accounts may offer a very low rate of interest (if any) but they are the most flexible in terms of accessing your money. Banks can also offer savings accounts, with higher interest rates, and also notice accounts with very competitive interest rates, but you may have to give a certain amount of notice before making a withdrawal (60 or 90 days perhaps), or you must agree to invest the money for a set period of time.

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**National Savings & Investments** – these products are backed by the government and operate like bank accounts to a certain extent. There are some tax-free products available and they are generally considered low risk since they are backed by the government.

**Bonds and Gilts -** Bond/Gilt Funds are generally considered to be lower risk than direct equity (share) investment although the value can still fall as well as rise. Bond markets can be split into two categories. Corporate bonds are investments based on business loans offered by private companies and are 'rated' based on the ability of the issuer to maintain interest payments and repay the loan. A corporate bond fund will invest in a wide range of these loans. 'Investment grade' stock within the fund is rated AAA to BBB, whilst stock rated a BB or below is termed 'junk or non-investment grade' and is sometimes referred to as 'High Yield'. Some funds also invest in Government Bonds (known as Gilts in the UK).

The income yield that is available from fixed income investments varies according to the quality of stock. Lower quality (junk or non-investment grade) stock usually offers a higher yield to attract investors (as they may be otherwise put off by the increased risk/volatility) whilst gilts generally offer much lower returns, they are underwritten by the government and so the risk of default is much reduced. As things stand, in order to achieve a reasonable yield without taking too great a risk an actively managed fund that invests in both gilts and corporate bonds (i.e. investment grade and high yield) represents the most suitable option.

**Property** – The long term historic performance of commercial property has very little correlation with the performance of corporate bond or equity based investments. For investors looking to diversify their portfolio property funds have historically offered attractive returns. Income from commercial property funds is often derived from contractually binding contracts of rent paid by business tenants to occupy property. Consequently leases are often arranged over a long period and generally include an 'upwards only clause' which ensures that rents are not negotiated downwards during the lease period, even in times of falling markets.

Added to the rental incomes, property has the added attraction of potentially appreciating in value over time, and although property values do fall, the 'bricks and mortar' assets of a fund remain. However, returns from a property fund are not guaranteed and the value of any investment can fall as well as rise. Also this market like all rental agreements, does not guarantee the tenants will or can pay rent as happened during the Covid19 pandemic.

Furthermore, because of the nature of property as an asset it may not always be possible to immediately switch or cash-in your investment, because the property in the fund may not always be readily saleable. If this is the case, then a fund manager may defer your request to cash in for a period of time. You should bear in mind that the valuation of property is a matter of the valuer's opinion, rather than a matter of fact.

**Equities (shares)** – Over the very long term equities have historically offered better returns for investors. Although this is not a guide to the future, it is felt that the increased risk of investing in company shares can potentially be rewarded by investment returns in excess of what is available from traditional bank or deposit accounts. However, there are no guarantees.

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**Investment 'Funds'** – Specialist investment managers will often manage a fund (a pool of investments) that invests in one or more of the above categories, the aim being to diversify the risk across a spread of shares, or bonds, or both. There are hundreds of investment funds available, each with their own specific aims and objectives. Investment funds can also specialise in one particular sector, such as only investing in companies that are listed on the FTSE100 index, or only investing in construction and mining companies. There are also funds that invest geographically, perhaps only buying shares in Japanese or American companies. Each sector has its own unique characteristics, and your adviser will be able to explain more about this.

All these types of investment are available through your financial adviser. You may be able to include your investment within a tax-efficient product such as NISA (New Individual Savings Account) or even a pension. There is a vast array of products available with which to save, and choosing the most suitable one can be difficult, so why not let your Financial Adviser help you to decide which is most suitable for you?

## Investing and Risk

**This section includes some of the good reasons for making investments into 'funds' run by 'fund managers' on behalf of the investors.**

Whether you are looking at investing in a pension, an investment bond or perhaps using a New Individual Savings Account (NISA) you might consider using investment funds. Put simply, a fund is a collection of many different people's money in one place. Buying large numbers of shares or achieving a portfolio of investments may well be beyond most average investors so they effectively club together to increase their purchasing power.

Typically, these pools of money are run and managed by an investment specialist. The manager is paid to make the day to day decisions of where the pooled money is invested. Rather than individuals (who have no interest in markets and shares, or who don't have the knowledge or time to study market information) choosing which shares to buy, to hold and to sell and at what time, the fund manager uses their expertise to make suitable investments in order for the value of the pooled fund to hopefully grow over time.

Another advantage of pooled investment is being able to diversify.

### Diversification and Risk

All investments carry some element of risk. The value of the fund can fall as well as rise and you may not get back the full amount you originally invest. To be able to manage the risks the manager will usually practice some level of 'diversification.' This works on the premise that holding 2 different shares is better than 2 of the same shares. This is because all shares react differently to investment conditions and changes.

For example, imagine that there are only 2 companies, one company making t-shirts and one company making woolly jumpers. If the weather forecast is for sunshine, then investors would be wise to buy shares in the t-shirt company as they expect demand for t-shirts to increase and sales to rise, increasing the company share price. However, we know that it is not always sunny and therefore a good manager would buy shares in both companies, so when one share price is static or even falling the other is able to support and perhaps offset the falls, meaning that the investor doesn't suffer a loss.



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www.warwickfs.co.uk

## Investment Assets

All investments carry some risk, and the Investing and Risk section above includes some information on how we might manage this risk. We can learn more about the particular risks and rewards of different investment funds by looking at their sector and assets in more detail.

All types of shares have different characteristics and these characteristics are complex. Hence there are fund managers within the industry that assess and measure these features and make investment decisions based on their knowledge and market experience.

Investment funds will have a particular aim, and often have a specialist sector which allows them to be compared to other funds of a similar make-up and ensures that the actual assets of the fund (the investments made by the fund manager on behalf of individual investors) remain in proportion with the selected aims and specification of the fund.

**Sectors and Assets -** The fund sector identifies broadly the areas in which the fund will invest. This can be based on geographical terms, or in a particular industry. For example, there are funds that only invest in UK companies, or Japanese companies, just as there are funds that invest purely in 'technology' companies (IT, telecoms etc). In addition to this there are sectors that are a mixture of assets. A typical 'balanced managed' fund will have some money invested in shares, some in property and some in fixed interest investments or bonds.

Although there are no guarantees as to performance or returns from any sector, our knowledge and experience can indicate how we might expect investments to perform.

**We will be able to explain risk in more detail. Contact us before making any decisions.**

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**The value of investments may fall as well as rise. You may get back less than you originally invested.**