

Best Advice

SUMMER 2009
EDITION

JULY 2009

Informed Choice Ltd

Special Points of Interest:

- Think carefully before investing your money. Does your financial adviser have a robust investment advice process in place?
- The FSA has published proposals to turn financial advice into a true profession.
- Academic research behind the passive investment argument looks flawed and actively managed funds can add greater value if they have a high 'active share'.

Welcome to the latest edition of our quarterly client newsletter—Best Advice.

Within this edition we cover a range of topics, including what to look for in a robust investment advice process, how retail financial services is finally becoming a profession, and an update on the active/passive fund management debate.

We also introduce our latest team member, Dermott Whelan, who joins us after roles in investment management with Morgan Stanley and Fidelity International.

We do hope that you enjoy reading this newsletter and we would welcome your feedback.

Do let us know if you have any questions.

Regards,

Nick & Martin

Nick Bamford & Martin Bamford
Joint Managing Directors



It's our 15th birthday!

We celebrate our 15th birthday on Saturday 11th July 2009.

Informed Choice was formed in 1994 and has gone from a small business run at a home office to one of the leading firms of Chartered Financial Planners in the UK.

Our continued success relies on our clients and we will strive to

continue delivering the high levels of service and advice they have come to expect over the years.

As we continue to grow our business, we would welcome the opportunity to speak to your family, friends or colleagues about their financial planning requirements. Please do put them in touch if we can help.



We are proud to be a Chartered firm of Independent Financial Advisers. This means we have satisfied rigorous criteria relating to professional qualifications and ethical good practice.

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Informed Choice Ltd are one of only five IFA firms in the UK to hold the Gold Standard for Independent Financial Advice—the toughest and most sought after award in financial services.

Best Advice

A robust investment advice process

After receiving a substantial inheritance I approached my existing IFA for some advice on how to invest the money. I have used this adviser in the past for mortgage and life insurance advice but when it comes to investment advice I am less confident in their recommendations. Should I seek a second opinion?

You are right to think very carefully before making a decision about investing your money. Investing is never easy, even with the assistance of an adviser, so you must be completely comfortable with any recommendations before exposing your capital to risk.

Fortunately, it is relatively straightforward to identify potentially unsuitable investment advice by spending a couple of minutes looking at the advice process. The delivery of consistently excellent investment advice requires that your IFA follows a process with at least the following six steps.

First, ask yourself if they understood your financial objectives. Linking any investment recommendations to your wider objectives is an important first measure before useful advice can be given. Unless your IFA understands the bigger picture, they cannot hope to provide advice relevant to your personal circumstances. How much time did your adviser spend discussing with you what you hope to achieve?

The second step in the investment advice process is understanding risk. It is your attitude towards risk, reward and volatility that will drive the suitability of any advice. Because risk is so subjective, it is simply not good enough for an IFA to quickly categorise you as a cautious, balanced or adventurous investor. These categories are meaningless without something substantial to back them up.

As an absolute minimum, your IFA should be having a detailed discussion with you about your attitude towards investment risk. A more robust approach involves the use of a psychometric questionnaire to explore your views on different elements of the subject.

Step number three is strategic asset allocation. Academic studies tell us that it is the broad asset classes in which you invest that make the most difference to the success of your portfolio, rather than the individual funds or stocks selected. Deciding on a strategic asset allocation model is therefore crucial to the long-term success of your investments. Ask your IFA how they have built your asset allocation model and what assumptions they have used.

Next, make tactical changes to the asset allocation model to reflect the view your IFA is taking on current economic and investment conditions. They may also recommend changes to take any of your existing investments, such as property ownership, into account.

Ask your IFA how they make these tactical decisions. For example, find out if they have an in-house investment committee or if they outsource this function.

Step number five is fund selection. There are no right or wrong answers here, as long as your IFA has a robust process in place to ensure the selection of suitable funds. They should be looking at a variety of factors to arrive at their recommendations and not simply relying on past performance figures or fund ratings.

Finally, the review strategy. Every investment should be reviewed at least annually to make sure it remains suitable. This is also a good opportunity to rebalance the asset allocation and find out if your attitude towards investment risk has changed over time. Ask your adviser about their review service and how this is paid for. This question should quickly identify those who are interested in the initial product sale rather than an ongoing relationship.

An IFA who can deliver excellent investment advice will have this or a very similar process firmly in place within their business. They will have no problems articulating the various steps in their investment advice process, in plain English and without resorting to technical waffle.

Your IFA should also have no qualms about you seeking a second opinion from a fellow professional. They should understand that this is a major financial decision for you to make which will have a lasting impact on your future financial prosperity.

Independent financial advice becomes a true profession

The publication last week of a consultation paper from the Financial Services Authority (FSA) contained proposals for turning financial advice into a true profession.

The paper contained three main proposals.

Firstly, your financial adviser will have to offer either 'independent advice' or 'restricted advice'.

Independent advice is a higher standard than currently offered by most independent financial advisers, but is a standard we here at Informed Choice have followed for the past five years. Restricted advice is that offered by the banks and multi-tied advisers.

Secondly, all financial advisers will need to have higher levels of professional qualifications.

The currently benchmark Certificate in Financial Planning will be replaced by a more demanding minimum of the Diploma in Financial Planning. There will also be a new code of ethics and a professional standards board.

Finally, so-called 'funded' commission where the product provider uses product charges to advance a large commission payment to the adviser, will be abolished by the end of 2012 to be replaced by 'adviser charging'.

This is the system of fee charging that we have been using since 2004 and ensures that the client understands precisely what they are paying for advice, implementation and review services.

These are all really positive proposals from the FSA and they will result in a much higher standard of advice for consumers. Naturally there will be firms within the retail financial services sector who resist these changes as they wish to maintain the status quo.

When is a guarantee not a guarantee?

So-called 'guaranteed' investment products are in the spotlight yet again, with a report from Which? Money concluding that they can be riskier than they appear.

These structured products often offer capital guarantees or '100% capital protection' regardless of what should happen to underlying investment markets. However, at the same time they provide contradictory information about the risks if the product provider or counter-party offering the capital protection were to go bust.

They also often come with a fixed end date which is used to calculate your investment returns. This means that you do not have any control over when to realise your investment returns, even if the markets have fallen at that time.

Finally (and perhaps most importantly) many of these products are not covered under the terms of the Financial Services Compensation Scheme (FSCS). This can leave investors with no protection should the firm offering capital protection, which is often a bank, was unable to meet their obligations.

Here at Informed Choice we do not recommend structured or 'guaranteed' products for all of the reasons listed above and because we feel they are an opaque investment option. Instead, our investment advice process is built around strategic asset allocation and the use of single-asset class collective investment funds.

Best Advice

The problem with the active/passive investment debate

At face value, it seems to be a simple debate.

Those investment advisers that back passive investment strategies like to talk about academic research proving this is a superior approach to active fund management. They point at the dozens of studies which have proven that active fund managers cannot outperform.

But what if this research was fundamentally flawed?

A closer look at the methodology behind many of these studies has found some serious problems.

Many of the earlier studies were based on a very small universe of actively managed funds. The very earliest studies looked at fewer than 200 funds; hardly a representative sample.

Choosing a benchmark for comparisons within these studies also proves problematic. Some studies compared large groups of style-specific funds with a broad market benchmark.

Possibly the biggest issue with the academic research used to back up the claims of passive investment advocates is the fact they look at one dimension of return - the tracking error. This means that have been comparing portfolio and index performance without making any qualitative assessment about the individual holdings of each one.

Research carried out at Yale University in October 2007 has added a new dimension to the passive/active debate after discovering that active fund managers can add value at the asset class level. The study, called '*How Active is Your Fund Manager?*', compared active fund holdings to benchmark index holdings. This resulted in an analysis of the 'active share' of each fund which is the net total of the implied long and short positions held comparable to the benchmark.

The conclusion of this Yale study is that active management needs to be measured in two dimensions; tracking error and active share.

The major finding was that funds with the highest active shares significantly outperform their benchmarks both before and after expenses.

So, the comparison between active and passive funds, as so often used by advocates of passive investment strategies, is flawed and potentially unfair. A better comparison would be between actively managed funds, pseudo-tracker funds (active funds with a low active share) and passive funds.

With the upcoming launch of the Vanguard range of passive funds in the UK market and news that HSBC is cutting the cost of its tracker funds to 0.25%, the active/passive debate is likely to be hotly debated over the coming months.

When listening to the arguments from the 'passive side', remember that evidence-based investing is only as good as the evidence used in the first place.

Introducing Dermott Whelan

We are pleased to introduce Dermott Whelan who joined the team as a Financial Planner at the start of June. Dermott was the founding member of Morgan Stanley's Discretionary Management team within its Private Wealth Division and launched their guided open-architecture multi-manager investment platform in 2007.



As part of the Investment Solutions Group at Fidelity International, Dermott was responsible for manager selection with a focus on European Equity and asset allocation.

In addition to his investment qualifications, Dermott is a Fellow of the Chartered Association of Certified Accountants and now holds the Diploma in Financial Planning. He is making rapid progress towards becoming a Chartered Financial Planner which is his goal by the end of this year.

This appointment is part of our strategy to grow the scale of Informed Choice. Since appointing Dermott to this role we have since recruited another Financial Planner to join the team, and we will be able to announce the details of this shortly.

If you know any top-quality financial advisers who would like to become a part of our award-winning firm, please do ask them to get in touch.

The new ISA rules

The introduction of a higher Individual Savings Account (ISA) annual limit in the April Budget speech has brought with it a degree of confusion over the new rules. Here is a brief explanation of much you are able to contribute to an ISA this tax year and next.

The new rules say that you can contribute up to £10,200 to an ISA each year from 6th April 2010 onwards. Some investors can invest this amount into an ISA during this tax year as well. The ISA limit for the current 2009/10 tax year is £7,200 until 6th October 2009 when it increases to £10,200 for investor who are 50 or older before 6th April 2010.

For investors over 50 who have utilised their full £7,200 ISA allowance at the start of this tax year, this means there will be an opportunity to invest a further £3,000 from 6th October 2009. For investors over 50 who are making regular contributions to their ISA, there is an opportunity to increase the monthly investment level without breaching the £7,200 limit before 6th October or the new £10,200 limit by 5th April 2010.

In terms of how the new £10,200 ISA limit can be allocated, this operates in the same 50:50 split as before. Up to £5,100 can be invested in the cash ISA component and the balance of the allowance can be invested in the investment ISA component. This means that, for example, if you decide to invest £2,000 in cash you can invest the remaining £8,200 of your £10,200 ISA allowance in investment funds.

Each part of your ISA allowance can only be invested with a single provider each tax year, but you can have multiple ISA providers (for cash and investments) over different tax years. We often recommend the use of a fund supermarket for our clients who are utilising their ISA allowance, as these offer access to a very wide range of funds from leading fund managers but all from a single provider.

Other than these changes, the ISA rules remain the same. All capital gains made within the ISA wrapper are free of capital gains tax. Investment income with an ISA is largely free of income tax, with the exception of the 10% tax credit on UK dividend income which cannot be reclaimed by ISA managers.

If you are 50 or over before 6th April 2010 it is worth making a note in your diary now as a reminder to revisit your ISA contributions after 6th October 2009 and before the end of the tax year. Do speak to us if you have any questions.

INFORMED CHOICE—NEWS IN BRIEF

- Saturday 11th July 2009 is the 15th birthday for Informed Choice after our formation in 1994. To celebrate our birthday we are giving away a Financial Plan worth £1,500 every day for 15 days. There are more details at www.informedchoice.ltd.uk/birthday.
- Our latest Investment Committee meeting took place at the start of July and we have now published our Investment Outlook report for Q3 2009. You can download this from our website at www.informedchoice.ltd.uk/investment.
- The Chartered Insurance Institute (CII) has revised the criteria for corporate Chartered Financial Planner status to ensure that this status remains at the pinnacle of the profession. We support the new criteria and already meet the new compulsory and discretionary criteria to continue using this valuable status.
- A number of exam results were received in June, with Philip Sullivan and Dermott Whelan both passing the Diploma in Financial Planning papers they took in April. Philip passed the investment principles module and Dermott passed all four Diploma modules which means he now has the Diploma in Financial Planning (DipPFS) from the Personal Finance Society.
- Our new consumer personal finance website—brilliantwithmoney.co.uk—is nearly ready for launch. This website aims to fill a gap in the market for personal finance education and will inform visitors about money management, savings and retirement planning using guides, blogs and videos.
- Informed Choice chartered financial planner Martin Bamford was named as one of the top media IFAs in the UK. He came in third place in the 2008 Media IFA of the Year awards. The award recognises advisers who regularly meet the requests of personal finance journalists, often at short notice.
- Andrew Neligan of Informed Choice has become a Certified Financial Planner (CFP) professional after passing his CFP assessment in April. He is in the process of applying to become a Chartered Financial Planner which will take the total number of Chartered Financial Planners at Informed Choice up to four.

Important Note:

This newsletter is provided for general consideration only and the information contained herein is not to be acted upon without professional independent financial advice.

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