MONEY
FINANCIAL TIMES PERSONAL FINANCE AND INVESTMENT

Saturday July 21 / Sunday July 22 2007

Financial Overview

Nicholas Kitchen, 42, a manager at an IT firm, and his wife, 44, a teacher, are interested in paying off more of their mortgage and saving into a wider variety of investment vehicles.

Annual income
Salary – £65,000
Spouse income – £10,000
Total – £75,000

Annual expenditure
Mortgage – £12,000
Utilities – £1,300
Council tax – £1,200
Expenses – £13,000
Savings – £10,000
Holidays – £5,000
Total – £42,500

Property, savings and investment
Home – £300,000
Unit-linked policies – £29,800
Investment Bond – £22,000
Cash account – £500
Endowment policy – £17,000
Total – £369,300

Insurance
Critical illness – four times salary
Death protection – £30,000
Spouse death cover – £80,000
Spouse critical illness cover – £75,000

Pensions
Company pension – currently worth £185,000
Spouse private pension – currently worth £12,000

Debt
Mortgage – £168,000
Credit card – £4,000
Total – £172,000

What should Kitchen do to achieve his goals?

James Norton, certified financial planner, Evolve Financial Planning

- Check what insurance is offered by employer
- Replace critical illness cover for income protection
- Consider overpaying mortgage each month

Jonathan Davis, chartered financial planner, Armstrong Davis

- Put portion of pension savings into cash fund
- Do not invest in property
- Put more savings into Isas

Miles Moseley, certified financial planner, MM Financial Management

- Make pension contributions in own name rather than spouse's for greater tax relief
- Gain broader fund selection
- Maintain mortgage and invest capital in equity

Once bitten, twice as likely to invest better

An IT manager who once made an untimely savings choice is now taking a closer look at important financial decisions

Elaine Moore
MONEY MAKEOVER

Seven years ago Nicholas Kitchen took the advice of a friend and put his savings into unit-linked savings policies and bonds. Unfortunately this coincided with a downturn in the stock market.

"I feel I might have been better off sticking the money under a mattress," he says. "I generally don't like paying fees and service charges, especially when I can't see the added value."

Kitchen has now started to educate himself in financial matters and pays much closer attention to the investments he makes.

Aside from an endowment policy worth £17,000 and £500 in cash, his assets are split between the savings policies and his £300,000 home.

"I lean towards longer-term investments," Kitchen says. "However, as my investments rise I may tend to be more conservative. Perhaps I should use bonds or predictable growth investments as a way to diversify."

Two years ago Kitchen borrowed £25,000 from his mortgage to put into an investment bond which has since dropped in value by £4,000. He now says that paying off more of his outstanding £168,000 mortgage is a priority. For the past two years his mortgage has been interest-only but is now repayment, which he pays off at the rate of £1,000 a month.

Kitchen, 42, and his wife, 44, want to know that the investments they have are efficient and that they have made the correct provisions for a comfortable retirement. They put aside around £10,000 each year from the salaries they earn as an IT manager and teacher respectively, and have built up retirement pots worth a combined total of £197,000.

The couple have no children and would like to retire at an age when they can still travel. They have considered living overseas where they believe they could enjoy a higher standard of living.

Financial Goals

- Have more money for holidays now
- Reduce outstanding mortgage
- Have a comfortable retirement

Jonathan Davis, chartered financial planner at Armstrong Davis, says that Kitchen's pension savings are perfectly adequate but he must consider a new strategy. Investing in equities has worked well for the past four years, but Davis recommends reducing exposure to equities and locking in the achieved growth. He says Kitchen should move around one-third of his pension assets to a cash fund while also reviewing his other savings.

Although Kitchen is interested in investing in property, his assets have not been sufficient in recent years to enable him to purchase another house. Property, according to Davis, is not the right place for Kitchen's energies. Instead he should put any additional savings into Isas.

Miles Moseley, certified financial planner at MM Financial Management, agrees that using vehicles such as Isas would help the couple save their money more tax efficiently.

He argues that they should utilise their pension relief allowances as much as possible and both use their £7,000 Isa allowances.

"It is arguably more efficient to make Isa contributions than pension contributions for a basic rate tax payer [such as Kitchen's wife]," says Moseley. "Clearly any pension saving that Kitchen's wife wishes to make should be made by Kitchen to obtain higher rate relief of 40 per cent."

Although Moseley is not overly concerned with Kitchen's high equity exposure, he says it is important to have an appropriate asset allocation and selection of investment funds.

Using their capital to pay off the mortgage rather than gain exposure to equity markets reduces their potential returns, notes Moseley. "It is better for medium/high-risk investors to maintain a mortgage for as long as possible and expose their capital to the equity market to obtain the best rate of return commensurate with their risk profile," he says.

James Norton, certified financial planner at Evolve Financial Planning, adds a note of caution. Although Kitchen rates himself as a high-risk investor, he wants to pay off his mortgage as soon as possible and this is a reasonable plan, thinks Norton. To make savings and investment a better decision than reducing mortgage payments, the couple would need to gain post-tax returns above their current mortgage rate of 4.5 per cent.

"Most mortgages allow you to overpay by at least £500 per month and this is something they should look to do," says Norton. "They should also consider cutting their losses on the bond and pay this off the mortgage too."

The financial impact of one partner dying would be significant. Both have elements of cover and Kitchen has death-in-service benefit of four times his income, but Norton advises them to obtain additional cover and go for income protection rather than critical illness cover, as it tends to be less expensive.

Some employers offer income protection benefits, sometimes covering up to 70 per cent of earnings. Kitchen should check to see if he has access to such a benefit and, if not, then he should take some out.