Financial Protection in Uncertain Times

words | Ian Le Breton

Last month this column offered up my now traditional "goodbye" to one year and "hello" to the next. As one sagacious reader rightly pointed out, I somehow managed to avoid making any firm predictions that might later be used in evidence against me. However the summary of my words might be: not such a bad year for many; strong signs of a recovery in certain places; people remain concerned about the future.

Since that column appeared, certain pieces in the complex jigsaw that makes up the global financial world have become even more difficult to place. Prices on global exchanges have been gyrating wildly. Ongoing problems in the UK and the continuing recession in the eurozone have resulted in several high profile companies going to the wall. Anyone hoping for a smoother financial ride in 2015 is likely to be in for a disappointment.

I therefore thought that, as we shake off the effects of Christmas and the New Year, it might be helpful to consider the steps people might take to protect themselves — or at least give themselves better peace of mind — in the increasingly turbulent seas through which we are sailing.

Whether one is considering currencies, interest rates or indeed the price of commodities, the market detests one thing above all else — uncertainty. And there can be no doubt that that we are living through uncertain, some might even say troubled, geopolitical and socio-economic times. The repercussions of these are likely to be felt in the first few months of 2015.

To take just one example: the price of crude

oil continued its spectacular downward trajectory in the early days of the New Year. The price of this strategically vital commodity has halved over the last six months. The UK chancellor welcomed the reduction because, despite being an oil producer, Britain will likely be a net beneficiary of lower energy prices. For some other countries — Venezuela and Russia are the most obvious — the price crash is creating real difficulties that, if prolonged, may have catastrophic consequences.

So what can we do to protect ourselves from turbulence, fear and uncertainty? You might perhaps consider insurance. The editor asked me to reference Valentine's Day, so now might be a good time to mention that if you are planning to acquire valuables or jewellery for your loved ones, it is essential to arrange cover in case of loss or damage. The first step should be to check your existing cover to find out whether it is up-to-date and adequate.

But a whole range of other risks can also be mitigated through insurance — from life, illness and accident through to transactional and tax insurance. As one of my Gibraltar-based insurance broking friends never ceases to remind me: "Almost anything can be insured — provided you are willing to pay the requisite premium." But insurance isn't always the answer. Read on.

For many, interest rates on mortgages, bank loans and credit card debts remain a major concern. Base rates in the UK and across the eurozone remain at record lows and there seems to be no immediate pressure to raise them — but therein lies the uncertainty. What if, due to some unforeseen economic shift, rates suddenly started to rise? Or what if banks, for instance, faced a further credit squeeze and there was simply no money for them to lend. Low interest rates would not mean a great deal if lending dried up.

One of the more popular criticisms of the UK banking sector in recent years — somewhat unfair in my view — is that banks have taken advantage of cheap money flooding into this system from quantitative easing to boost their balance sheets rather than lending out the funds as intended. It is certainly the case that not all this money has been passed on, but given the increased liquidity ratios demanded by central banks, not to mention the various "stress tests" to which banks have been subjected, it is not easy to see how else they could have behaved.

So if you're a borrower, now might be a good time to look at the interest rates you are being charged and see what deals are available to "fix" your mortgage rates for the longer term or re-finance other borrowings. It is also always good to reduce credit card debt too, perhaps by way of "consolidation". Naturally if you are effectively a "lender" — that is your savings outweigh your borrowings — then, by the same token, you should ensure that you are maximising your returns. Remember however that the security of your capital is paramount, so yield should always be balanced against risk.

Currency markets are also very unstable at present. In Gibraltar, most of us "think" in pounds so we should consider its performance in recent months. Against the euro it remains relatively strong but that has perhaps the result more of euro weakness than sterling strength. The US dollar has performed very strongly against both currencies recently. If you are planning a major transaction in a foreign currency — a property transaction or an investment abroad — some type of "forward deal" to fix the exchange rate might be appropriate. Professional advice should always be sought but the added peace of mind may well be worth the effort.

I should also note the current spectre of deflation. This is not something anyone my age (or younger) has had to consider in the UK until now. I grew up in the certainty that prices would rise remorselessly every year. But in the euro zone an overall fall in prices of 0.2% was reported for the year to December 2014. Granted an inflation rate of 0.6% would have been applied had energy prices not fallen by 6.3% over the year, but why is deflation a bad thing?

Surely we would all be better off if things cost less tomorrow than they do today? "Up to a point, Lord Copper." The danger with deflation is that consumers delay or even stop spending in the hope that prices next month will be lower. If this continues for some time, demand drops and businesses cut production and lay off staff. This in turn leads to decreased demand and a vicious circle is created: falling prices, declining wages and debt burdens increasing. Let us hope that the threat of deflation remains just that: a theoretical concept. Or, to put it another way, don't delay buying that jewellery for your valentine. Your economy needs you!

So what else should we be doing in these uncertain times? We should be doing all we can to protect the lifestyle that we currently enjoy against the vagaries of the future, particularly in terms of our retirement. The UK in particular is about to experience wholesale changes in the pensions market, so it has never been more important to take responsibility for planning your own future.

The days of people retiring in their fifties on "gold plated" final salary schemes are likely gone forever. Add to that the widening gap between retirement age and increased life expectancy and it's obvious that the average retirement age will have to increase. Checking on your existing pension arrangements — and then seeking sound advice — should be high on everyone's financial "to do" list.

I should finish with a quick word about companies and the enhanced protection that setting up your own corporate structure can provide. The internet age has reversed a trend that has held sway since the industrial revolution first drove people into factories, by enabling ever increasing numbers of people to become self-employed. However such freedom carries risks and the limited liability offered by a private company is something that should not be overlooked. True, a company director can be sued if things go wrong but there is protection for that too — directors' and officers' liability insurance. Using companies in this way is a subject I will cover in a future article.

We may not be able to control the financial markets or the events happening around the world, but we can all take practical steps as individuals that might enable us to take just a little more control of our — and our families — financial future. ■

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