Understanding cash and its role in your financial plan

High street banks and building societies are slowly increasing the interest rates available on their savings accounts. Whilst these can look like a good way of contributing to your financial goals, holding too much of your savings in cash can have a very negative impact on your overall return.

Here are **four good reasons** to remain invested:

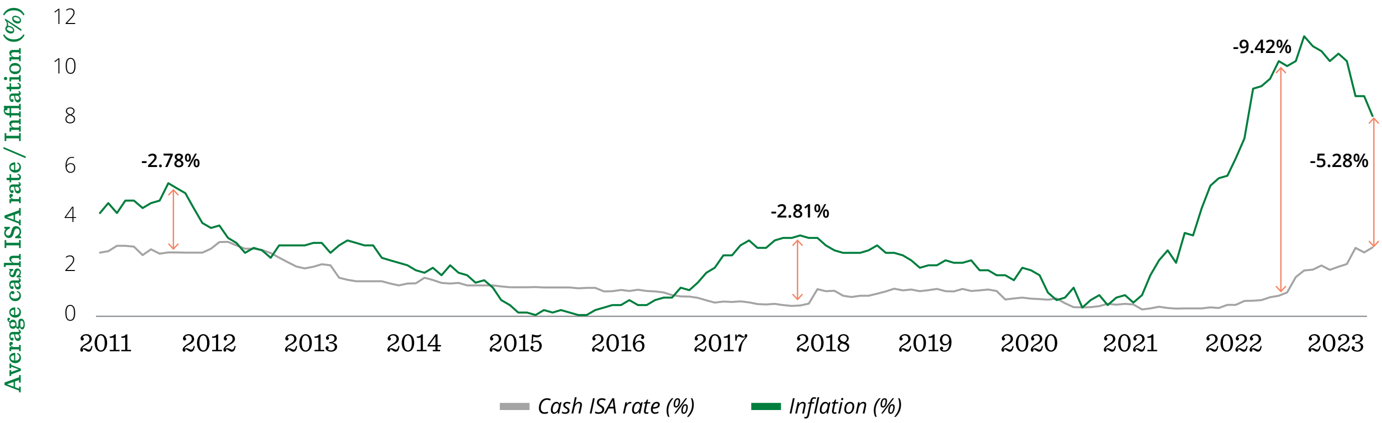
1. Mind the gap - holding cash will erode the value of your savings

A key part of any financial plan is to consider how you can protect your hard-earned savings from the ravages of inflation.

With the Bank of England (BoE) raising interest rates to 5% in July 2023, savers should be seeing greater returns from their cash. However, many banks and building societies, while quick to raise mortgage rates, have yet to meaningfully up their interest rates on products such as cash ISAs.

As a result of this inaction and inflation remaining stubbornly high, savers are realising a loss of more than 5% due to the gap between saving rates and inflation, according to our analysis.

The chart below shows the gap between interest rates and inflation this year is at its largest for more than a decade.



Source: Cash ISA rate (monthly interest rate of UK monetary financial institutions sterling cash ISA deposits including unconditional bonuses), Bank of England Database, 30 June 2023 and UK CPI, ONS, 19 July 2023.

Earning interest on your cash that is below the rate of inflation guarantees a loss on your money in real terms.

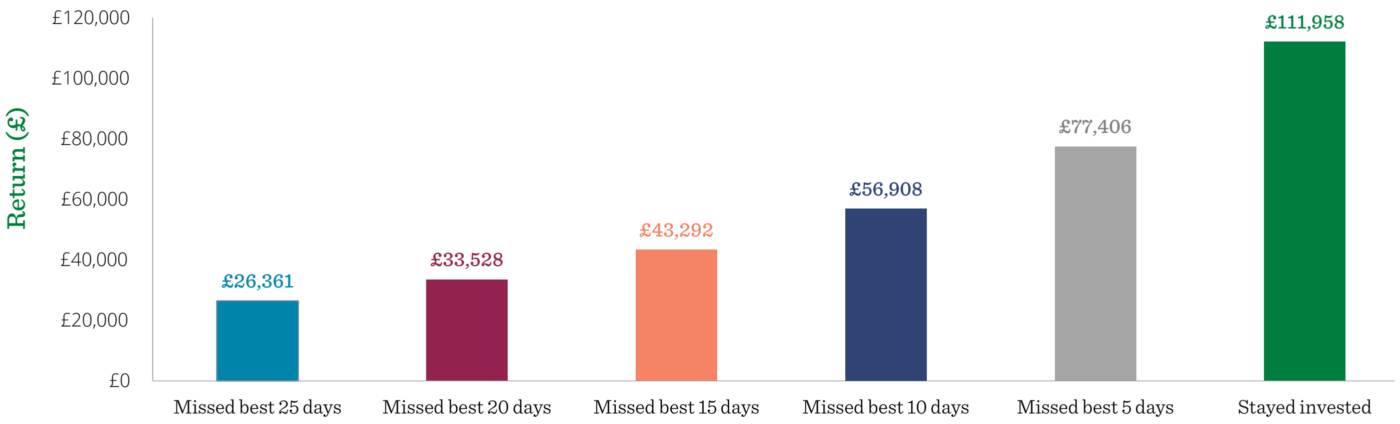
2. Don't miss out - stock markets tend to rally after high inflation

Markets can turn quickly and being out of the market for even a short period of time can significantly reduce your returns.

Interest rates and inflation are currently higher than they have been for some time. However, history shows that after about 18-24 months, interest rates will usually dampen inflation, and both will start to drop.

History has shown that when this happens, stocks and shares typically begin to rise. Markets can turn quickly and missing the best days can significantly reduce your overall returns. Remaining invested, if you can, will maximise your chance of benefiting from this potential future increase.

The chart below shows that staying invested in global equities over the past 30 years, could have delivered a potential return more than four times greater than that of an investor who missed the best 25 days during the same period.



Source: Quilter Investors as at 30 June 2023. Total return in pounds sterling over period 30 June 1993 to 30 June 2023. Based on initial investment of £10,000 into the MSCI All Country World Index. The information provided is for illustrative purposes only and doesn't represent the past performance of any particular investment. It is not possible to invest directly into an index.

Time in the market is usually more successful than trying to time the market. Missing just a few of the best days in the stock market can significantly reduce how much your investment grows.

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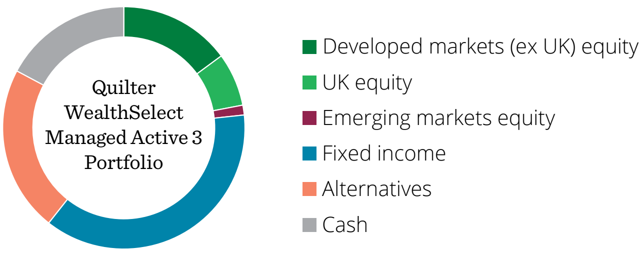
3. Part of the plan - cash is often already included in a diversified investment portfolio

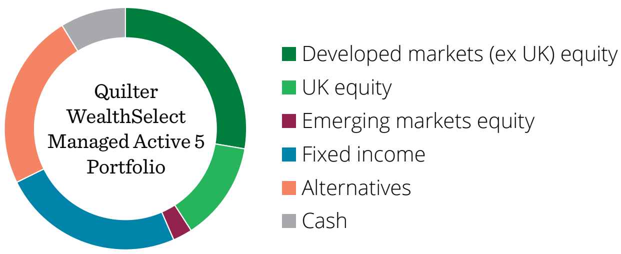
If you invest in a Quilter WealthSelect portfolio, your portfolio manager will already have some cash exposure in your diversified portfolio (depending on your appetite for risk). There will typically be a higher allocation to cash in lower-risk portfolios.

The charts below show the different levels of cash held in two of the WealthSelect Managed Portfolios.

Asset allocation



Asset allocation



Source: Quilter Investors as at 30 June 2023

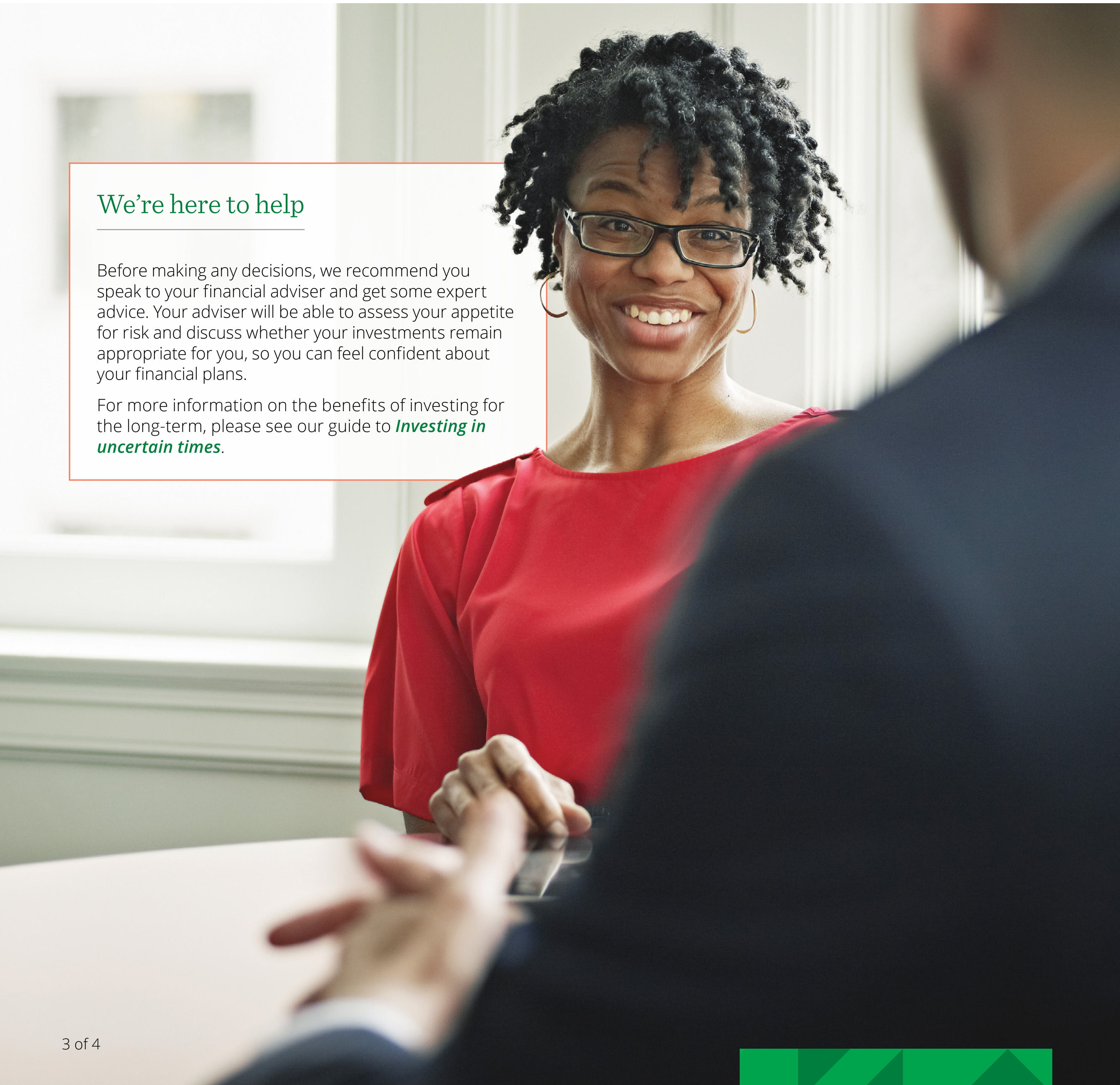
When investing in cash, portfolio managers will usually invest in money market funds, which have the benefit of being managed by a professional. This approach also gives the portfolio manager the flexibility to move out of cash and into other assets quickly if market conditions changes.

The WealthSelect portfolio management team are experienced in understanding the economic environment and how much cash it's appropriate to hold to achieve good long-term returns.

4. Beware of the taxman - general savings accounts are not tax-free

If you are investing outside of a cash ISA, interest earned on banks and building society savings accounts are subject to tax. Those with wages, pension, or other income above £17,570 will only have the Personal Savings Allowance (PSA) available to help them before they start paying tax on the interest they receive[3]. The PSA is £1,000 for a basic rate taxpayer, £500 for higher rate taxpayers, and £0 for additional rate taxpayers. Anything earned above the PSA will be taxed at your marginal rate.

At 4% interest, a higher rate taxpayer would only need to hold £12,500 in a general savings account before they were taxed on the interest.



We're here to help

Before making any decisions, we recommend you speak to your financial adviser and get some expert advice. Your adviser will be able to assess your appetite for risk and discuss whether your investments remain appropriate for you, so you can feel confident about your financial plans.

For more information on the benefits of investing for the long-term, please see our guide to ***Investing in uncertain times***.

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