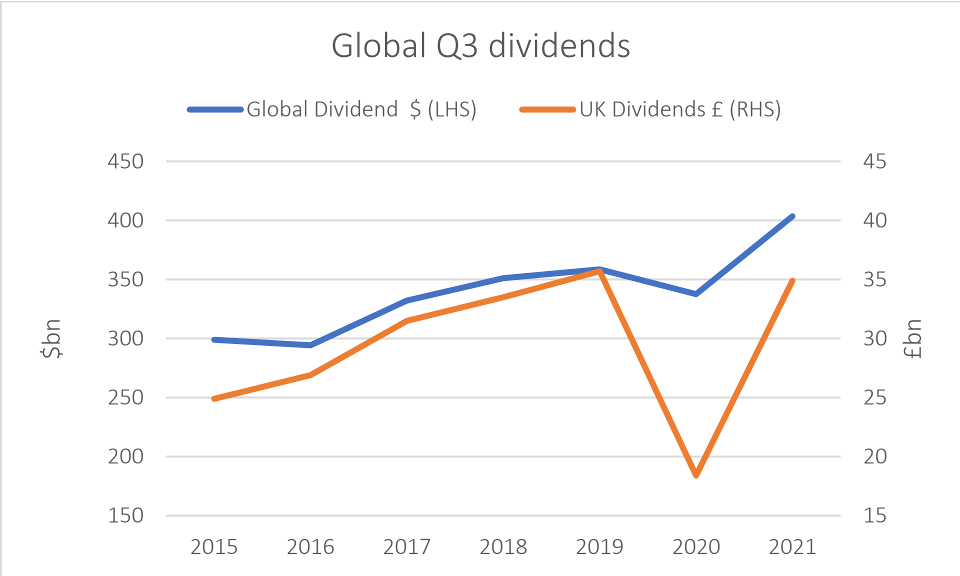
The global dividend recovery

Research shows that in Q3 2021, dividend payments increased sharply in all major markets and are expected to return to pre-pandemic levels before the year's end.



Sources: Janus Henderson, Link Group.

In 2020, global dividends fell by 11.9% year-on-year in USD terms according to an index calculated by the investment manager Janus Henderson. In the UK, dividends suffered a much greater drop, with a decline of 42.9% recorded by Link Group, a leading corporate services provider. The UK's significant underperformance had much to do with the Bank of England forcing UK banks to suspend dividend payments.

Both Janus Henderson and Link Group recently published their latest dividend reports covering the third quarter of 2021. The gloom that pervaded 2020 had disappeared:

- On a global basis, overall dividend payments jumped a record 22.0% year-on-year to an all-time high for the third quarter of the year.
- In the UK, total dividend payments were 89.2% higher than in the same period of 2020.

Both sets of figures were helped by a boom in dividends from mining companies, which accounted for two thirds of the increase in global dividends according to Janus Henderson's calculations. The biggest global dividend payer in the third quarter – and likely for the whole of 2021 – is BHP, an Australian miner whose shares are currently listed in both London and Sydney.

In the UK, miners took the top three positions in the dividend payers' league for Q3 2021. Five mining companies paid special (one-off) dividends totalling £4.3 billion, about £1 in £8 of all dividend payments over the quarter. The result was that the concentration of dividend payments among a small number of companies in the UK grew significantly – just five companies (including that trio of miners) accounted for over half of Q3 dividends.

On a global basis, Janus Henderson expects dividends to surpass their pre-pandemic peak by the end of the year, a rapid recovery from their low point in March. While Link Group estimate that 2021 UK dividends will be 45% higher than 2020's, that would still be 17.4% below the level of 2019.

If you are looking for income, these latest sets of dividend data are a reminder of the power of companies to generate income for their investors.

Universal Credit eligibility expands to higher rate taxpayers

Autumn Budget reforms have created a surprising clash of benefits and income tax.

The Covid-19 pandemic was the first time many people utilised Universal Credit (UC) for the first time – between February and May 2020, the number of households claiming UC rose by 1.7 million to 4.2 million. In March 2020, the UC standard allowance was temporarily increased by the equivalent of £1,000 a year, but in October 2021, that extra payment came to an end. In its place, the Budget contained announcements of two UC improvements that are now in effect:

- All working elements were increased by £500 a year, meaning that an extra £500 of net income can be earned before any clawback of UC started; and
- The rate of clawback was reduced from 63% to 55%. As a result, if an extra £100 of net income is received and this leads to a reduction in UC payments, the loss of UC will be £55 rather than the previous £63.

So what?

The Institute for Fiscal Studies (IFS) has looked at this question and produced a surprising answer. The lower taper rate, applying to a higher starting point, now means that it is possible for higher rate taxpayers to be eligible for UC, a situation that once only applied in Scotland, where the higher rate threshold is £6,608 lower than in the rest of the UK.

One example the IFS gave is that a single earner couple with two children and monthly rent of £750 could have earnings of up to £58,900 a year in 2020/21 before losing all their UC entitlement – £9,600 more than before the Budget announcement. Not only is that ceiling well into the higher rate tax band, it is also above the £50,000 level at which the notorious High Income Child Benefit Tax Charge begins to take effect.

There are many assumptions underlying that IFS calculation, not the least of which is that the couple are not disqualified from any UC entitlement by having savings of above £16,000. In practice, the IFS calculates that 26% of all families will be entitled to UC, a proportion that rises to 84% for lone parents.

The interaction of the tapering of UC, higher rate tax and child benefit tax is complex. If you think you might be caught by that trio, make sure you understand the ramifications – you might find an extra £100 of gross earnings are worth less than £10 net.

Escaping the higher minimum pension age

A surprise change of tack on pension ages was revealed when this year's Finance Bill was published.

In February 2021, the government confirmed that it would go ahead with a two-year increase in the normal minimum pension age (NMPA) from 55 to 57 from April 2028. The NMPA is the earliest age at which you can start to draw benefits from a pension arrangement, unless you are covered by a limited range of exemptions.

The news coincided with the publication of a consultation document which by July had resulted in draft clauses for this year's Finance Bill. One part of the draft that surprised some pension experts was that the proposed legislation allowed people with an actual or prospective right to retire between age 55 and 57 to transfer their pension to a new provider with their existing pension age safeguarded. However, the transfer had to occur by 5 April 2023. As many personal pensions set their minimum benefit age equal to the NMPA, there was a concern that the legislation would encourage buy-now-while-stocks-last pension transfers merely to lock in age 55.

The Finance Bill, published on 4 November 2021, closed off this option by limiting it to transfers made before that date. The move was a surprise – there was no hint of the change in the Budget – but it was nevertheless welcomed by many pension organisations. The Economic Secretary to the Treasury justified the lack of any notice by explaining that a prior warning "could have led to unnecessary turbulence in the pensions market". Other longer-standing concessions on early retirement ages remain in force.

In practice, a pension age of 55 – still legally possible if you reach that age before 6 April 2028 – is only a viable option if you have a large pension pot and, preferably, other sources of income. For example, at age 55 the current lifetime allowance of £1,073,100 would buy an inflation-proofed pension of under £1,500 a month (before tax). A level pension would be much higher – about £3,500 a month – but could you live for 30 years or more with no pension increases?

The Investment COACH

Demerging China from emerging markets

Some investment professionals are calling for China to be removed from the main emerging markets indices.

The MSCI Emerging Markets Index is the leading emerging markets (EM) index, with over 1,400 constituents covering 26 countries. The value of investment capital either tracking or benchmarked against it measures in the trillions of dollars, a following that means any changes to the index have potentially wide implications. Likewise, large adjustments could be particularly disruptive as many investment managers would have to buy and sell shares to mirror the revised structure of the index.

This problem raised its head a few years ago as MSCI decided to increase the weighting of China in the index. Although the country remains under-represented in the index, it already accounts for nearly 35% (as at the end of October 2021). The next largest constituent country, ironically Taiwan, counts for 14.7%.

China's weighting in the index has doubled over the last five years, although at present much of this is through Chinese companies, such as Alibaba, whose shares are listed outside China. In time, China could account for over 40% of the index.

Recently, Goldman Sachs, the major US investment bank, published a paper examining whether the time had arrived to separate China from the EM index it was coming to dominate. The authors of the paper argued that China deserved to stand alone for a variety of reasons, including:

- It has the second largest global equity market after the US, worth $18 trillion with nearly 6,000 listed stocks.
- It dominates the EM index and is already has the largest single country weighting in the index's history.
- China is a country subject to "idiosyncratic factors". This is the bankers' careful way of saying that the country of President Xi Jinping has a different geopolitical stance from many other EM countries and, of late, a somewhat unpredictable regulatory policy.

The paper has provoked much comment and served as a useful reminder of two facts for individual investors in the UK:

- China is too big a market to ignore; and
- If you are investing in index-tracking funds, it pays to understand what the underlying constituents are.

England’s social care cost cap

More details have emerged on the £86,000 social care cost cap for England.

At the start of September, the Prime Minister announced long-awaited plans for the funding of social care in England (Wales, Scotland and Northern Ireland all have their own social care funding regimes). Alongside the announcement came the news of a new Health and Social Care Levy, effectively adding 1.25 percentage points to the National Insurance contributions of employers, employees and the self-employed throughout the UK from April 2022.

Two of the key features of the proposals, due to start in October 2023, were:

- New higher capital limits for means testing. The upper limit, above which you must pay for all your care, would rise from the current £23,250 to £100,000 and the lower limit, where your care costs are fully funded by your local authority, would rise from £14,250 to £20,000.
- An £86,000 cap on personal care costs paid, above which you would not have to make any contribution to your care costs.

In mid-November, the government revealed more information on how the cap would work in practice. It is less generous that had been expected:

- The cap only applies to your personal care costs, not living costs, such as accommodation and food. These will be assumed to be £200 a week for care home residents and normally must be met by the resident.
- Any top-up fees paid for superior facilities are ignored – everything is pegged to the local authority cost.
- Crucially, the cap is based on care payments made by you, but not the total care cost borne by you and your local authority, as had been expected.

The third point means that if you have capital of £106,000 or more, you could find yourself paying up to the cap to meet your care costs. Below that level of wealth, the risk is that you will pay until you reach the £20,000 lower capital threshold.

The cost-conscious hand of the Treasury has been blamed for the new interpretation of the fee cap. Whether or not that is true, the change is a reminder that the potential cost of care still needs to be built into your retirement plans.