2022 investment wrap-up

In 2022, most of the world's major share indices had their worst year since 2008, but the UK's FTSE 100 was a star performer.

Index	2022 Change
FTSE 100	+0.9%
FTSE 250	-19.7%
Dow Jones Industrial	-9.2%
Standard & Poor's 500	-19.8%
Nikkei 225	-9.4%
Euro Stoxx 50 (€)	-11.7%
Shanghai Composite	-15.1%
MSCI Emerging Markets (£)	-12.6%

Yes, the table is correct. In the year of three Prime Ministers, four Chancellors, a catastrophic 'mini-Budget' and double-digit inflation, the UK stock market was one of the world's best major market performers, eking out a small gain where most others recorded a loss. The MSCI All Country World Index – a good benchmark for Global plc – fell by 9.7% in sterling terms.

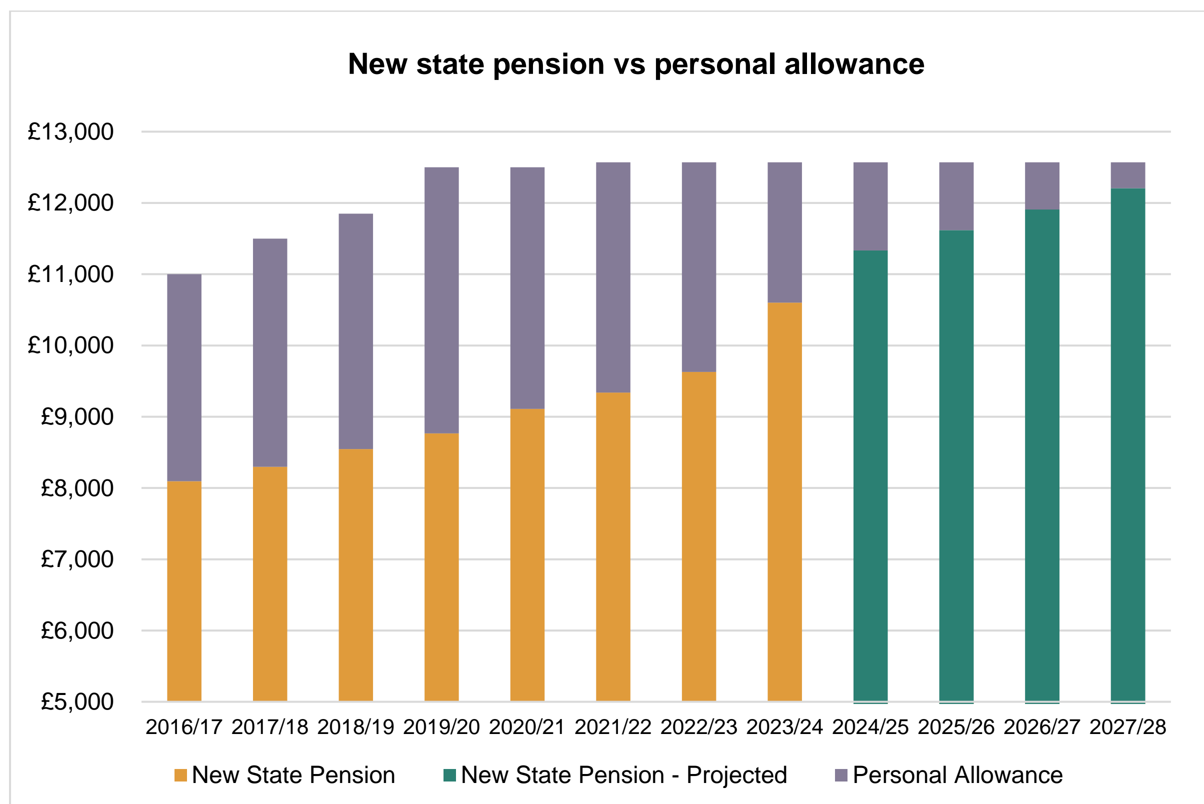
Inevitably, such a surprise result from the UK comes with some important qualifications:

- The yardstick that shows the UK posting a positive return is the FTSE 100, which only covers the largest 100 UK listed companies. Look at the broadest UK index, the FTSE All-Share, and there was a loss of 3.2%.
- While the FTSE 100 is an index of companies listed on the London Stock Exchange, it is far from a snapshot of UK plc. About 14% of the index is accounted for by three energy companies – Shell alone accounts for over 9%. The basic resources sector provides just over 9%, albeit its constituents do not have their mines in the UK.
- The 250 mid-sized companies that form the FTSE 250 and sit below the FTSE 100 are closer to what most people would consider UK plc. As the table shows, this group had a tough 2022 – just what might be expected given the state of the UK economy.
- While the FTSE 100 outperformed the US and Eurozone, the gap is not so wide when currency performance is considered. Sterling fell 11.2% against the US dollar and 5.4% against the euro.
- On the plus side, if you had re-invested all the FTSE 100 dividends over the year, your return would have been 4.7%, a reminder that the UK stock market remains a good source of income.

The UK's winning streak in 2022 – at least in FTSE 100 terms – does not mean you should now ignore investment diversification. After all, the FTSE 100 was way behind the best performing global market of the year. That title, with a jump of over 100% in sterling terms, belonged to a country with over 80% inflation – Turkey.

Into the ice age: the diminishing personal allowance

The frozen personal allowance may be overtaken by the new state pension in only a few years, proving the income tax screw is well and truly tightening.



Source: DWP, HMRC, OBR.

The new state pension, payable to eligible individuals who reached their State Pension age after 5 April 2016, will rise by 10.1% to £203.85 a week in April 2023 – that is £10,600 a year. The increase is once again in line with the Triple Lock, which uprates the main state pensions by the greatest of:

- consumer price index (CPI) inflation;
- earnings growth; and
- 2.5%.

Of all three indicators, CPI was the clear winner this time around, as earnings have failed to keep pace with soaring price inflation.

While many other state benefits will also grow by 10.1%, the mirroring of inflation by the DWP is not matched by another government department – HMRC. The personal allowance will stay at £12,570 in April 2023, remaining at its two-year-old frozen level. It was due to start rising again from April 2026, but the Chancellor's latest Autumn Statement added another two years to that date, meaning the personal allowance will be frozen up to and including 2027/28 – a total freeze of six tax years.

The impact of that lengthy ice age is demonstrated in the chart above. What this shows is the new state pension from when it began in 2016/17 to 2023/24 (orange) and the Office for Budget Responsibility's (OBR) projections for the level over the following four years (green). The purple element shows the gap between the personal allowance and state pension in each tax year. In 2019/20, the personal allowance was over £3,700 higher than the new state pension.

If – a big *if* – the OBR's crystal ball is wholly accurate, then by 2027/28 the difference will be about £360 – less than a tenth as much. The OBR's estimate only needs to undershoot by 0.8% a year for the new state pension to be larger than the personal allowance in 2027/28. That could cause problems for HMRC, because although the state pension is taxable, it is paid without deduction of tax.

Of course, it may not happen – 2027/28 is well after the next election, for a start. However, it is a reminder both of how the income tax screw is being turned tighter and why income tax planning is becoming ever more important.

Company cars: not-so-free fuel

If your employer pays for the fuel in your company car, it may cost you more than you expect.

As the Autumn Statement was not a Budget, detailed publications that would normally emerge as the Chancellor sat down have taken time to appear. For example, the HMRC projections of how many more capital gains tax (CGT) payers there would be because of the much-reduced annual exemption (another 570,000 by 2024/25) did not appear until the Monday after the Autumn Statement, missing the weekend personal finance pages.

One even later arrival – three weeks after the Autumn Statement – was an HMRC bulletin on the fuel benefit charge for company cars in 2023/24. For some years the basis has been an increase in line with September annual CPI inflation (published in mid-October), so there was no explicit reason for HMRC's procrastination. The number that was eventually revealed was the current figure, increased by 10.1%, as had been expected.

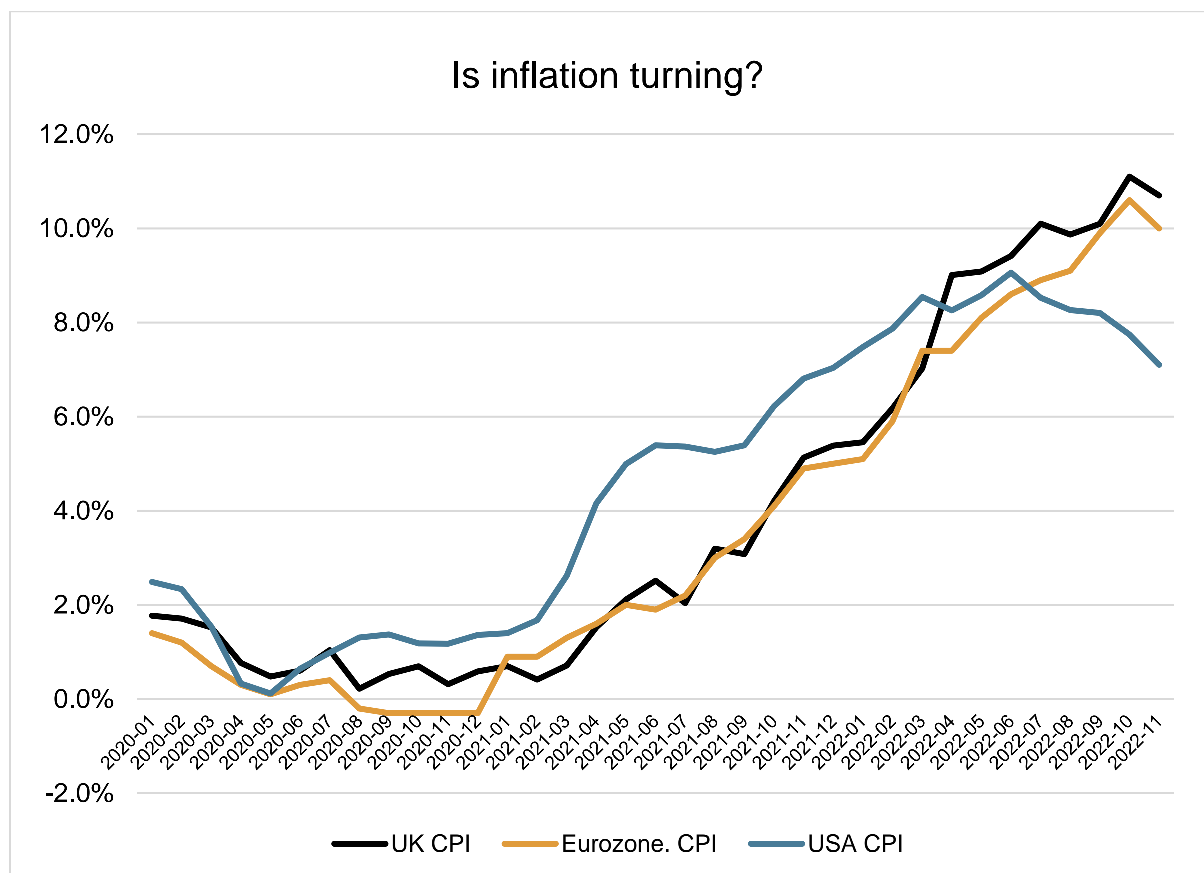
That means for 2023/24 if you have 'free' fuel, its taxable value will be assessed by multiplying £27,800 by your car's percentage scale charge. For example, if you have a petrol-engine car with CO_2 emissions of 130–134 g/km, your scale charge is 31% and £8,618 (£27,800 x 31%) will be added to your income for tax purposes. In terms of hard cash, that is an extra £3,447 going to the Exchequer if you are a 40% taxpayer.

At this point you are probably wondering how far £3,447 of petrol would take you. Assume a price of £1.60 a litre and 40 miles a gallon and the answer is about 19,000 miles. In 2019, before the pandemic disrupted travel, the average car covered 7,400 miles a year. If that figure still applies – and it is probably less because of increased working from home – then the 'free' fuel break-even point is more than 250% of typical use.

Not all benefits are so harshly taxed – electric cars can be an attractive option – but the large cost of 'free' fuel is a reminder that when it comes to anything financial, 'free' is a word to be treated with great caution.

2023 inflation forecast: the only way is down?

Inflation surged in 2022, but can it reverse in 2023?



Source: ONS, Eurostat, BLS.

Forecasters of inflation were way off target for 2022. For example:

- In December 2021, the Bank of England's Monetary Policy Committee said "CPI inflation was expected to remain around 5% through the majority of the winter period, and peak at around 6% in April 2022".
- Two months earlier, the Office for Budget Responsibility (OBR) in its Economic and Fiscal Outlook said "News since we closed our forecast would be consistent with inflation peaking at close to 5% next year. And it could hit the highest rate seen in the UK for three decades".

The OBR was a decade out. At the time of writing, it looks as if the peak 2022 reading for UK CPI inflation was October's 11.1% – the highest for 41 years according to the Office for National Statistics. Is that the peak for this inflationary cycle, as the data in the graph above hints?

The good news is that, as of now, inflation does look set to drop. Some of that is down to what economists call the 'base effect'. Annual inflation is the difference between prices, 12 months apart, so each new month's inflation calculation loses the oldest month of data which is

replaced by the latest month. If the month that disappears was one in which there was an inflation spike and the new month is spike free, then inflation falls.

For example, in the month of April 2022, prices rose by 2.5% because of the utility price cap increase. If April 2023 sees monthly price rises of a still high 1.0%, then annual inflation will drop by 1.5% (2.5% – 1.0%).

Some commodity and service prices have already fallen from the highs created by Covid-19 supply issues and/or the Ukraine war and these drops will work through to domestic inflation. For example, by mid-December the price of wheat had almost halved from its February peak. Shipping costs have also fallen dramatically from their 2022 highs.

One point to remember is that a falling inflation rate does not mean overall prices are falling, so your financial planning may well need a review to take account of the damage inflicted by 2022's CPI.