Beckford · James

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Glossary of Terms

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This glossary provides a quick introduction to the terms and phrases you are likely to encounter when investing through Beckford James.

The explanation of any type of investment, product wrapper or service in this guide does not imply its suitability or recommendation. Some investments are only available to experienced investors and may not be suitable for all clients - you should always consult your adviser before investing. Risks may apply to any of the product wrappers or investments mentioned and you should speak to your adviser for more information on these. More information on the risks of investing can be found in the Key Features Document. Any explanation offered in this document is subject to our understanding of English law and taxation legislation. You should consult your adviser for more information on how tax may affect you and your investments as this will depend upon your personal circumstances.

Accumulation Units/Shares

A class of units or shares of an open ended investment that enables distributions, usually dividends, to be accumulated within the investment rather than paid out as income. Once ‘accumulated’ the distribution is reflected in the price of the units or shares.

Accumulated distributions are still treated as income for tax purposes and should be declared as income in the annual HMRC self-assessment tax form.

Some investments do not offer an accumulation option. In such cases, where distributions are paid, they can still be retained within the investment and used to buy additional units or shares.

Alpha

A measure of risk adjusted performance of an investment compared to a benchmark index. Alpha is usually interpreted as representative of the value that an investment manager adds to the return from an investment. For example, if an investment manager outperforms a risk adjusted benchmark, the fund will have positive alpha. If the fund falls below the benchmark it will have negative alpha. It is an integral element of widely used Modern Portfolio Theory statistics and can be found within fund factsheets and investment research tools.

In any analysis of an investment using such statistics, Alpha should be assessed with reference to:

- Beta - the measure of an investment’s volatility in relation to the market, and
- R squared - the degree to which an investment’s performance is attributable to the performance of the benchmark index.

Annuity

In pension terminology, an annuity is most commonly simply a contract provided by an insurance company under which a retiree exchanges all, or part, of their pension fund for an income for the remainder of that person’s life. In some cases, at least in part, this includes the lifetime of a surviving beneficiary such as a spouse. Many annuities also provide for a ‘guarantee period’ of say five or 10 years to offer some protection to a surviving beneficiary against the annuitant’s premature death.

An annuity can usually be paid monthly, quarterly, half yearly or annually.

The annuity income may be level, remaining unchanged throughout the payment period, irrespective of inflation or changes in circumstances. Otherwise, it may include the provision for automatic annual increases. This could be a fixed percentage per annum or the annual change in, say, the Retail Prices Index.

The amount of the annuity is dependent upon mortality, gender (in some cases), health (in some cases) and the underlying yields on fixed interest securities, specifically 15 year gilts. Understandably, annuity rates rise with age, and those in poor health with lower life expectancy can often secure superior rates.

The annuity contract is known technically as a secured pension. Once purchased, the decision is normally irreversible. Therefore purchasing an annuity is sometimes perceived as an inflexible option leading to an increasing interest in unsecured pensions, or 'income drawdown', where an income is drawn from the accumulated pension fund, with no mortality assumptions factored in.

Income from a pension annuity is taxed as earned income under PAYE rules. It is possible to purchase a non-pension annuity with monies held outside approved pension arrangements. These may provide a lifetime income or an income for a specified period. In such instances, part of the income is deemed to be a return of capital and is therefore non-taxable.

Asset Allocation

The division of an investment portfolio between different asset classes. In its broadest definition, 'strategic' asset allocation defines the relative exposure of a portfolio to:

- cash (liquid investments such as bank deposits)
- bonds (fixed interest securities)
- equities (shares).

More in depth asset allocations will sub-divide these broad classes into narrower categories. For example, bonds by:

- provider (eg British government or international corporate organisation)
- duration (eg short, medium or long term)
- yield (investment grade, sub-investment grade, 'junk').

In the case of equities this may be by:

- investment objective (eg value, core, growth)
- market capitalisation (eg large, medium, small cap)
- geography (eg UK Equities or International Equities).

Modern Portfolio Theory maintains that asset allocation is critical to efficient and effective investment strategy, accounting for up to 90% or even 95% of a portfolio's return.

The principle is that the investor should aim to achieve an asset allocation that will offer the optimal potential return for a given level of risk. The range of such asset allocations is expressed statistically as the efficient return.

Grounded in the theory is the principle of diversification. This states that as various asset types behave differently in a particular market environment, a spread of assets across the categories over time will not only reduce risk exposure, but may also improve return prospects.

Authorised Fund

In the UK, a collective investment fund, such as a unit trust or Open Ended Investment Company which is subject to authorisation and regulation by the Financial Conduct Authority (FCA) under the Financial Services and Markets Act 2000 and the Financial Services Act 2012. This means certain regulatory rules apply in terms of the how the fund is run and invested. This includes restrictions on what the investment manager may invest in, rules on reporting and accounting and to which investors the fund may be marketed.

Balanced Funds

Investments that offer exposure to a mix of asset classes, typically designed to mitigate risk through diversification.

Therefore, an adviser may use a 'balanced fund' to meet a client's target asset allocation based on a selected risk profile.

With any balanced fund, it is important to identify and monitor the asset mix within the investment to ensure that it is appropriate to an investor's needs, especially if it is being recommended in isolation. This is because the actual asset mix and, therefore, the risk characteristics of balanced funds may vary considerably from one investment to another and from time to time.

Benefit Crystallisation

The act of converting accumulated investments, held within a pension scheme, into benefits. In the case of a UK approved pension scheme, such as a SIPP, these benefits may consist of up to 25% of the pension fund as tax free cash and a taxable income, either as income drawdown or the purchase of an annuity. Benefits from UK pensions are subject to rules and regulations imposed by HMRC.

Although changes made to the UK pension regulations were designed to simplify the rules, they remain complex and you should refer to HMRC or a tax specialist if in any doubt. In simple terms, you are deemed to have 'crystallised' the benefit of any part of the accumulated pension fund when you decide to convert this into cash, regular income or a lifetime annuity purchased on the open market. The decision to crystallise is irreversible.

Beta

A measure of the volatility of an investment in relation to the market, as defined by a benchmark index. The Beta coefficient measures the systematic risk of an investment, i.e. how the investment is likely to respond to fluctuations in the returns of its benchmark index.

- a beta of one means that the investment should move in line with the index
- a beta of more than one indicates higher volatility than the index
- less than one indicates lower volatility.

Beta is an integral element of Modern Portfolio Theory statistics and can be found within fund factsheets and investment research tools.

In any analysis of an investment using these statistics, Beta should be assessed with reference to Alpha and R squared (both are explained in this glossary).

Bid-Offer Spread

The differential, usually expressed as a percentage, between the purchase and sale price of an investment. The 'bid-offer spread' can most commonly be seen as the characteristic pricing structure of a unit trust. The percentage difference between the two prices provides an indication of the initial, i.e. upfront cost of investing.

The higher Offer (or 'Ask') Price is the price at which units are 'offered' for sale by the fund company; the lower Bid (or 'Sell') price indicates the price at which the investor can sell units.

Bid-Offer Spread, also commonly known as dual pricing is an integral element of the cost of purchasing an investment. Typically, it reflects capital costs incurred in managing a fund, incorporating marketing (including introductory charges) and other management expenses. The offer price is negotiable and it is possible in many cases to agree discounts.

The term is also used in relation to individual equities where it is expressed as a monetary amount and reflects trading costs.

For information about other investment costs and charges, see also Total Expense Ratio.

Bond (1)

In investment terms, bond usually relates to fixed interest securities, such as British Government bonds (Gilts) or corporate bonds, also known as loan stock. This is where an investor essentially 'lends' their money to an institution which, in return, undertakes to pay a certain rate of interest (the coupon) for a specified period. The institution agrees to return the investment at 'par', eg in the case of Gilts, £100 for every £100 of nominal stock purchased. This is, technically, a 'contract of trust'.

Bond (2)

Bond can also relate to other contractual investments, including life funds provided by insurance companies and fixed term or guaranteed return and structured products issued by banks and building societies. See Investment Bonds.

CETV/CEV

Deferred final salary (defined benefit) scheme benefits are normally expressed as a deferred pension at the date of leaving which will be revalued in line with statutory requirements until the member's normal retirement date. The lump sum value of these benefits in today's terms is calculated by the scheme and expressed as a Cash Equivalent (Transfer) Value (CETV or CEV). If transferred, this value has to grow by a certain rate to provide a fund to match the benefits that could be obtained outside the scheme and this figure if often obtained using a Transfer Value Analysis (TVAS). The comparison should explain the rates of return that would have to be achieved to replicate the benefits being given up. In this context, the commonly-used industry phrase is 'critical yield' to describe these rates required.

Capital Gains Tax (CGT)

A tax on realised gains or profits on real property, shares or other investments.

All gains up to an annual allowance are taxed at 0%; a tax rate of 18% (or 28%) will apply on all gains over and above the annual allowance and once added to your marginal income tax rate.

The ‘chargeable gain’ is calculated by subtracting the sale proceeds from the acquisition cost. However, specific rules apply in terms of determining the acquisition cost for assets purchased prior to 05 April 1998.

More information about CGT can be found on the HMRC site at www.hmrc.gov.uk/

There are several ways that an individual can mitigate against CGT, for example by holding assets jointly so that any gain is ‘shared’ between the holders and by taking advantage of ‘tax sheltered’ investments such as Individual Savings Accounts (ISAs) or Pensions. CGT is not chargeable on life funds but gains may incur an income tax liability.

Closed Ended

Closed ended investments offer a fixed amount of shares in the fund to investors. A set amount of shares are issued when the investment is launched and these shares can then be bought and sold on the secondary market. This means that further shares cannot be created, or cancelled, by the investment manager, as is the case with open ended investments such as OEICs.

Closed ended funds include Investment Trusts. The shares in these investments trade on the LSE, where the price is determined by supply and demand given the fact that a fixed amount of shares are in circulation. As no further shares can be created the fund is known as closed ended.

Corporate Action

The act of making substantive changes to an investment, such as a collective fund or share. This may involve changes to the name, features and structure of an investment, such as a company rights issue or a change of fund type or investment strategy. This will include mergers, acquisitions or closures. Where significant corporate actions take place, Novia will undertake to communicate this to investors to inform them of the change and any options and/or actions that may result.

You can find details of corporate actions applicable to investments available through Novia here. You should check this page regularly to keep up to date with any corporate actions that could affect investments you hold through the service.

Critical Yield

1 Drawdown Pensions
Critical yields are illustrated by product providers using a common prescribed basis. There are two types (A and B).

Type A – the growth rate needed on the “drawdown” investment sufficient to provide and maintain an income equal to that obtainable under an equivalent immediate annuity.

Type B – the growth rates necessary to provide and maintain the actual level of income chosen.

2 Occupational Pension Transfers
The value of the benefits of a deferred final salary (defined benefit) scheme is calculated by the scheme and expressed as a Cash Equivalent Transfer Value (CETV). On transfer this value has to grow by a certain level and this figure if often obtained using a Transfer Value Analysis (TVAS). The comparison should explain the rates of return that would have to be achieved to replicate the benefits being given up. In this context, the commonly-used industry phrase is ‘critical yield’ to describe these rates required.

Current Yield

The current value of interest distributions paid out by a bond (fixed interest security) or bond fund as a percentage of the current market value. It is calculated by dividing the latest annual interest payment by the current market price.

Custody

The safe keeping of investments, including details of where and by whom it is registered and where these records are maintained. Custody records may be in respect of stock exchange traded investments like shares, investment trusts and ETFs or directly traded unit trusts and OEICs.

Historically, share or fund certificates declaring the details of the owner and holding were issued so that custody rested with the individual investor.

Today, very few 'physical' investment transactions take place. Therefore, sales and purchases are settled and registered electronically. Typically, investments are held on the client's behalf by a nominee company. This offers greater efficiency and security and is more cost effective.

All transactions processed through Novia are electronic. Investments are held by Novia nominee companies which act as custodian, holding the investments in safe-keeping on behalf of the investor, who ultimately owns the investment at all times.

Derivative

A financial instrument designed for specific, strategic investment purposes. The purpose may be to hedge against a specific risk or to speculate. The basic principle behind derivatives is that they enable investors to make gains in both rising and falling markets. Thus, traders use derivatives to mitigate market risks as well as to give them the opportunity to make major gains. The downside of this may be the potential for major losses - even greater than the investment made - if the strategy backfires.

Each derivative is based on an underlying asset which may be financial, i.e. a stock, bond or market index, or a commodity such as gold, oil or an agricultural crop; its price is derived from the price of this underlying source.

Commonly used derivatives include 'futures' (agreement to buy a specified amount of the underlying asset at a future date at a specified price) and 'options' (agreement which gives a buyer the right, but not the obligation, to buy a specified amount of the asset at a future date at a specified price, and vice versa for a seller).

Dilution Levy

A levy which may be imposed by the investment manager of a collective fund, usually a unit trust, on large purchases or sales. This is where such transactions may create greater expenses for, or impose constraints on, the fund that might disadvantage other investors. The dilution levy is designed to offset any such effects and thereby ensure that other investors are not disadvantaged.

Distribution

Payments to holders of collective investment vehicles, such as unit trusts or OEICs, made from the income generated by the underlying assets held by the fund. The income will typically comprise dividends from equity holdings and interest from bonds (fixed interest securities), less any expenses deducted by the investment manager. It is important to bear in mind that some funds deduct costs and expenses from the capital value of the fund whereas others deduct them from income distributions. Distributions are usually paid out six monthly although some funds pay out monthly, quarterly or yearly.

Income distributions can be either paid out as a cash payment or re-invested. Some funds offer the option of:

- an income version (unit/share class) where distributions are automatically paid out as cash
- or an accumulation version (unit/share class) where distributions are automatically reinvested to increase the price of each unit or share.

Other funds that do not have income and accumulation versions offer the option of reinvesting distributions to purchase additional units or shares.

Life and pensions funds do not provide distributions of income. All interest and dividends are retained within the fund. Life funds do offer the facility to generate an 'income' through periodic encashment of units.

Dividend

An income, representing a share of net profits, paid by a company to its shareholders in return for their ownership of part of the equity of the company. Dividends are typically distributed half yearly, although some larger companies declare quarterly. There is no obligation upon any company to declare a dividend.

The rate of dividends will often indicate the nature and style of a company. For example, companies targeting fast and significant growth will typically declare very small or zero dividends, since their strategy will be to re-invest profits to aid the growth. Conversely, one of the main attractions to shareholders in well-established, profitable value companies may well be a regular, steadily growing dividend stream.

Dividends are paid out of net profits and special tax rules apply to investors. Non-taxpayers, pension funds and ISA investors are no longer able to reclaim the tax credit on the net dividend. This tax credit is deemed to discharge the individual investor's basic rate tax liability. For a higher (40%) rate taxpayer, the net dividend has to be 'grossed up' by the 10% tax credit, and an additional 22.5% tax liability applies on the resultant gross figure (i.e. a total tax of 32.5%).

You can find more information on dividend taxation at: www.direct.gov.uk

Dividend Yield

Dividend yield measures in percentage terms, the annual dividends distributed by a company or equity fund. It is calculated by dividing the last year's annual dividends per share by the current share price.

Dual Pricing

A pricing structure for an investment that provides for two prices, i.e. an offer price at which an investor can buy shares or units and a bid price at which the investor sells them. The difference between the two prices is known as the Bid-Offer Spread. Dual pricing applies to most unit trusts, but usually not to other open ended funds such as OEICs - where a single price structure normally applies.

Equity

A share of the ownership of a particular asset. In investment terms, usually related to a company share or share-backed fund, or property.

Exchange Traded Fund (ETF)

An investment fund, tracking a sector or index, that is traded on a stock exchange. An ETF typically trades at a price which is very close to its net asset value, unlike an investment trust. This means that you can usually be confident that the price of an ETF very closely reflects the value of the investments it holds and sector or index it tracks.

Essentially, an ETF offers the benefits of a collective investment fund yet trades on a stock exchange like a share. Most track a specific stock market index such as the FTSE 100 or FTSE All Share.

ETFs are characterised by low costs and stock-like features. They have been available in the US since 1993. In the UK they were seen as of limited appeal until a recent advantageous change in Stamp Duty rules made them a more attractive and cost efficient method of investing in a particular index than passively managed funds.

The most widely used form of ETFs in the UK are iShares operated by Barclays Global Investors. It is important to bear in mind that iShares are domiciled in Dublin so that there is no UK tax credit, which may mean that a UK investor will incur an additional tax charge on dividends. However, ETFs can be held within a stocks and shares ISA or SIPP, thereby sheltering the dividends against tax.

Through Novia you may purchase iShares and many other ETFs available on the London Stock Exchange (LSE).

Ex-Dividend

The time between the end of a period used for calculating the next dividend on an investment and the date at which that dividend is distributed to investors.

Where an investor acquires a holding in an investment during an ex-dividend period, they will not be entitled to receive the next (imminent) dividend distribution. In these circumstances, the purchase is 'ex-dividend'.

The price of any income-producing investment fund will include a factor that broadly represents the dividends that have accrued from underlying assets during the dividend period. Therefore, it is common for the price to fall once the investment fund goes ex-dividend. This trend is most pronounced in higher income producing investment funds where the income payments are a significant factor in the decision to buy.

Financial Express Crown Rating

A quantitative ratings system developed by Financial Express designed to highlight funds that have consistently superior performance in relation to risk relative to their peer groups and fund sectors (as defined by the IMA, the Investment Management Association and the ABI, the Association of British Insurers).

Crown Ratings are compiled using three key measurements of a fund's performance:

- alpha relative to the sector, measured over three years
- volatility
- consistency.

In most cases, each of the constituents is weighted equally. Alpha and volatility are measured over three years but with a higher weighting given to more recent performance. Consistency is based on a fund's performance ranking within its sector in each quarter of the three years. Each quarter is weighted equally.
For more information see www.financialexpress.net

FCA

The Financial Conduct Authority is a statutory body established by the Financial Services and Markets Act 2000 (FSMA) and the Financial Services Act 2012. Their aim is to ensure financial markets work well so consumers get a fair deal and they have set out the following three statutory objectives:

- protect consumers;
- enhance the integrity of the UK financial system; and
- help maintain the competitive markets and promote effective competition in the interests of consumers.

These are supported by six principles of good regulation to which the FCA pays regard in discharging its statutory obligations:

- efficiency and economy, the need to use our resources in the most efficient and economical way. The Treasury is able to commission value-for-money reviews of our operations which are important controls over our efficiency and economy.

- proportionality, the principle that a burden or restriction imposed on a person or activity should be proportionate to the benefits which are expected to result. In making judgements in this area, we take into account the costs to firms and consumers. One of the main techniques we use is cost-benefit analysis of proposed regulatory requirements. This approach is shown, in particular, in the different regulatory requirements we apply to wholesale and retail markets.

- responsibility of consumers, the general principle that consumers should take responsibility for their decisions.

- responsibility of senior management to comply with the regulatory framework, a firm's senior management is responsible for its activities and for ensuring that its business complies with regulatory requirements. This principle is designed to secure an adequate but proportionate level of regulatory intervention by holding senior management responsible for risk management and controls within firms. Accordingly, firms must take reasonable care to make it clear who has what responsibility and to ensure that the affairs of the firm can be adequately monitored and controlled.

- openness and disclosure, publishing information about regulated persons or requiring them to publish information, which underlines the importance of us making market information available, with appropriate safeguards, to reinforce market discipline and the desirability of enhancing the understanding of members of the public in their financial matters.

- transparency, we should exercise our functions as transparently as possible, which recognises the importance of ensuring that appropriate information is provided on regulatory decisions and also that the FCA should be open and accessible, both to the regulated community and the general public.

Novia is authorised and regulated by the Financial Conduct Authority.

For more information on the FCA, its statutory obligations and principles of good regulation, you can visit the FCA website at http://www.fca.org.uk/

GIA

General Investment Account. A general purpose product wrapper to hold a wide range of investments, for example shares, unit trusts or OEICs not held within an ISA, Offshore Bond or SIPP.

Hedge Fund

A private investment fund often open to a limited range of investors which undertakes a wider range of activities than other investment funds and which typically pays a performance fee to its manager. Typically, these funds are not FCA authorised and therefore not regulated in their activities.

Hedge funds may invest in a broad range of investments, from shares, debt and commodities to works of art.

The original purpose of hedge funds may have been to reflect their name by offsetting potential losses in investment markets through hedging. However the tendency over recent years has been to use the investment techniques inherent in hedging strategies to increase returns so that the attraction to many investors is in the potential for absolute returns, however the wider market moves. This may include in particular short selling, leverage and other investment techniques.

Hedge funds are unregulated in terms of their leveraging activities and fee structures and although many hedge fund managers reside in London, the funds they manage are domiciled offshore. The typical hedge fund investor is a wealthy individual or experienced investor.

Any restriction in the scope of a hedge fund manager’s activities is likely to be voluntary and based on its arrangements with its investors.

Hedge funds employ a number of different trading strategies and styles. The most common is long/short equity which combines long equity positions hedged with short sales and/or index options.

Other strategies include investing in emerging markets, sector funds, fundamental growth and value and distressed securities.

Whilst hedge funds can be seen as obscure and shrouded in mystery, a more accessible structure has emerged in the guise of Funds of Hedge Funds, which are more widely accessible. These can provide broad exposure to the hedge fund market and thereby achieve a measure of risk control through diversification. However, Fund of Hedge Funds have been criticised for high costs and charges.

ICVC

Investment Company with Variable Capital. Effectively an alternative name for an OEIC, and therefore an open ended collective investment fund. As with other collective investments this enables an investor to benefit from the economies of scale of pooled investing and from professional day to day management of a wide collection of assets.

Information Ratio

A statistical measure of risk adjusted return widely used in analysing equity funds.

Information Ratio is calculated by dividing the annualised relative return (i.e. the return on the fund versus its benchmark) by the annualised relative risk.

It is used as a measure of the consistency by which a fund outperforms its benchmark and captures 'direct fund management risk', i.e. risk that cannot be attributed to the benchmark.

A higher information ratio signifies outperformance.

In-specie Transfer

The act of transferring assets from one investment platform or product wrapper provider to another, without converting those assets into cash form. In this way, technically no disposal of the investments has taken place, and the investor is not 'out of the market' for a period of time whilst selling and buying.

In-specie transfer can be used to minimise transaction costs and for strategic or tax planning purposes.

Interest

Income distributions paid to investors on cash and money market accounts, bonds (fixed interest) and bond funds.

Interest is normally paid net of tax at 20%. An investor who is liable to tax at the higher marginal 40% tax rate will be liable to an additional 20% tax on interest, which is collected via the annual HMRC self assessment procedure.

Investment Bonds - Offshore/Onshore

Investment funds held within a life fund product wrapper, domiciled either within the UK or in an offshore setting. Known as Investment Bonds, or 'single premium, non-qualifying policies of life assurance' these funds take advantage of the specific tax rules applicable to life policies.

These funds do not distribute income by way of dividends or interest but the investor can generate an 'income' from regular encashment of units. This facility is commonly used in tax deferral strategies, in particular taking advantage of the facility to withdraw up to 5% of the original capital without incurring immediate tax liability for up to 20 years.

Although the investor does not pay CGT on gains made within life funds, part or total encashments may incur an income tax liability for a higher rate taxpayer at the difference between basic and higher rate tax. A realised gain on a life fund may have the effect of 'pushing' an individual into the higher rate tax band. The tax calculation to determine the rate applicable to gains is carried out under what is known as 'top slicing' rules.

The change to a single CGT tax rate of 18%, combined with the regime of internal taxation of income and gains have been widely construed as making onshore life funds less attractive from an investment and tax planning perspective for many investors, compared to offshore life funds and other collective investments where internal taxation does not apply. The investor could consider the benefits of the offshore life fund compared to the onshore life fund where internal taxation of income and gains applies but where gains are subject only to higher rate tax liability.

Novia offers an Offshore Bond, provided by Royal London 360 Insurance Company Limited in the Isle of Man.

Investment Trust

A closed ended collective investment vehicle which enables an investor to manage risk through investment diversification and the professional day to day management of a portfolio of assets.

The primary difference between an investment trust and its open ended equivalents, unit trusts and OEICs, lies in the structure of the investment fund. An investment trust is itself a company in which the investor buys shares, which are traded on a stock exchange.

Therefore, the price of an investment trust will not necessarily reflect the net asset value of the underlying assets. Therefore, at any point, the price of the shares in an investment trust are said to trade at a 'premium' - above the net asset value, or at a 'discount' - below this level.

An investment trust manager can also borrow against the value of the investment fund to maximise potential returns, known as 'gearing'.

This means that the investment trust structure can be seen as potentially beneficial for enhancing returns but also fundamentally higher risk with greater short term fluctuations in value, as the price of the trust moves to reflect market volatility.

For more information see the Association of Investment Companies site at www.theaic.co.uk

ISA

Individual Savings Account: a product wrapper that provides tax free returns on cash or stock market investments.

ISAs were introduced in April 1999. Since then, the terms and conditions have been simplified significantly so that for this tax year, the following rules apply:

- The maximum ISA annual allowance for the year is £15,000 (2014/15)
- You can subscribe to either a stocks and shares ISA or a cash ISA, or in any combination of amounts between the two, up to the overall annual limit of £15,000
- You are only able to open one cash and one stocks and shares ISA each tax year (with the same or different providers) up to the annual limit
- You are able to hold tax-free cash within a stocks & shares ISA as well as a cash ISA
- You can switch or transfer funds from a cash to stocks and shares ISA and vice versa

Returns from ISAs are free from personal tax liability, but the tax credit of 10% on UK share dividends is non-reclaimable by an ISA manager.

ISA Manager

A commonly used, and regulatory, term for a company that offers management and administration services for an Individual Savings Account (ISA) product wrapper and is registered to provide such services by HMRC. Novia acts as the ISA manager for the cash ISA and stocks and shares ISA available to investors through the Novia service.

As with Novia, the ISA Manager may not be responsible for management of the underlying investments held within the ISA product wrapper.

ISA Transfer

An ISA holding which is transferred from a previous ISA product wrapper provider, in cash, to a new ISA. ISAs may be transferred in this manner.

ISIN

The International Security Identification Number (ISIN) is a global system used to uniquely identify equities and other securities (such as bonds) traded on stock exchanges around the world.

KFD – Key Features Document

The key features document (KFD) gives consumers the main points about any financial product or service they are considering purchasing without having to resort to the fine print. The KFD must include key headings outlining the product, its features, benefits, aims, risks and the requirements the consumer has to meet as well as a Q&A section. Although no two KFDs are exactly alike (each product requires a bespoke KFD), the FSA issues guidelines for how financial services companies should present the KFD to prospective customers.

Kiid – Key Investor Information Document

The majority of funds must now provide a Key Investor Information Document to investors, which displays an ongoing charge figure rather than the total expense ratio, as part of European regulation.

The KIID, which replaces the simplified prospectus, is a two-page document that provides detail about the fund's objective and investment policy, risk and reward, charges and past performance.

Leveraging (Gearing)

In investment terms, a process designed to maximise returns where the investment manager is empowered to borrow against the assets of an investment fund or utilise 'shorting'. This is effectively gaining additional returns by leveraging assets that the investment fund does not actually own.

Gearing is commonplace in closed ended funds, such as Investment Trusts. Until recently it has not been permissible as an investment strategy in open-ended funds. However, investment funds complying with the certain directives are able to gear to some degree and this has led to the emergence of a new generation of open ended funds, such as absolute return funds.

LSE

London Stock Exchange: commonly known as the LSE, this is the UK's premier and largest stock trading exchange. The LSE is globally renowned and acknowledged.

The 'regulated' LSE was founded in 1801 with a formal, subscription based membership. In 1973, women were admitted for the first time and in 1988 the so-called 'Big Bang' signalled the deregulation of the market.

Over its history, the Exchange has been rocked by many scandals and collapses in prices and confidence, from the South Seas Bubble in 1820, though the Wall Street Crash of 1929, the subsequent crashes of 1973 and 1987 to the sub-prime mortgage and banking crisis of 2007 and 2008. However, the Exchange has remained open for business whatever the financial and economic climate, and has never shut down purely as a response to a run on the market.

Through Novia you may access equities traded on the LSE. More information on equity trading through Novia is available here.

For more information, you can visit the LSE website at www.londonstockexchange.com

MEX code

A unique identification code commonly used for open ended funds and UK life and pension funds (see ISIN, SEDOL). Unlike other identifiers, the MEX code consists of a series of letters.

Modern Portfolio Theory (MPT)

First promoted by mathematician Harry Markowitz in his paper 'Portfolio Selection', which appeared in the 1952 Journal of Finance. 38 years later, he shared a Nobel Prize with Merton Miller and William Sharpe for what has become a broad and almost universally accepted theory for portfolio selection.

Prior to Markowitz's work, investors focused on assessing the risk and returns from each individual component of an investment portfolio. Therefore, if a specific security type or sector appeared to offer the best opportunities at a particular point in time, the investor's portfolio might well be made up entirely from this narrow sector.

Even though this might seem clearly unwise, it was commonplace before the introduction of diversification which lies at the heart of MPT. For the first time he showed in formal terms, the mathematics of diversification. This showed that investors, rather than focus on the 'best' sector or asset type at a specific time, should construct portfolios based on their overall risk-reward characteristics, and should build portfolios rather than 'cherry pick' individual stocks.

Central to Markowitz's theory was the principle that out of the entire spread of possible portfolios, certain ones will optimally balance risk and reward.

Modern Portfolio Theory provides a context and framework for investors and advisers to understand systemic risk and reward by using statistical analysis and data, such as Alpha, Beta, R-squared and Sharpe Ratio.

Morningstar OBSR Analyst Rating TM

A method of analysing and measuring the quality of investment funds based on qualitative principles. Morningstar OBSR (Old Broad Street Research) specialises in rating the universe of UK open ended funds, i.e. unit trusts and OEICs. The Morningstar OBSR research team of qualified investment professionals conducts a proven, robust and independent due diligence process where qualitative research, focusing on an investment manager interview is supported by quantitative analysis of risk and return statistics.

Once the due diligence process has been concluded, a fund can be categorised and is then eligible to be considered for a Morningstar OBSR Analyst Rating. Relevant funds are presented to and evaluated by the Morningstar OBSR Fund Rating Committee. They use the same methodology to arrive at all ratings. They do not work to a "quota" nor are they paid to rate funds. The number of rated funds is simply the result of their due diligence process. Any fund which receives a positive Morningstar OBSR Analyst Rating is exceptional of its type.

Morningstar OBSR's fund ratings are part of a global scale that identifies positive as well as negative Analyst Ratings. These are Gold, Silver and Bronze. Neutral and Negative are two additional designations to offer investors more information. The Morningstar OBSR Analyst Rating is based on Morningstar OBSR analysts' convictions in a fund's ability to outperform its peer group and/or relevant benchmark on a risk-adjusted basis over the long term.

More information is available at http://www.morningstar-obsr.co.uk/

Mortality Drag

If you purchase an annuity, you may benefit from a cross subsidy from those annuitants that die relatively early. This cross subsidy is not present with Unsecured Income plans (Drawdown et al) and so to provide a comparable income, a higher investment return will be required. The impact of mortality can be expressed as an annual percentage rate by which the net investment performance of the remaining personal pension fund would have to exceed the interest rate implicit in an annuity in order to break even. This effect has become known as the 'mortality drag'.

NISA – "New ISA" – see ISA

Nominee Account

A custodial account held on a client's behalf by a third party but established for the absolute benefit of the customer.

Holding investments within a nominee account enables transactions to be carried out speedily and cost effectively and helps to ensure comprehensive, up to date and robust record keeping. In particular, the economies of scale provided by a service such as Novia, using a Nominee Account system, allows investment funds to be purchased at very significant discounts. It enables the adviser to build, manage and monitor client assets and portfolios in a cost and time efficient manner.

OCF – Ongoing Charge Figure

This is the new term for the total expense ratio (TER) and it gives the most accurate measure of what it costs to invest in a fund. The OCF is made up of the annual management charge (AMC) and other operating costs.

The AMC is levied by the manager and is used to pay the investment manager, fund accountant, administrator and distributor. Other operating costs include those for extra services paid for by the fund, such as the fees paid to the trustee (or depositary), auditor and regulator etc.

OEIC

An open ended collective investment vehicle, enabling an investor to manage risk through investment diversification and the professional day to day management of a portfolio of assets.

An OEIC is established under company law and is run by a Board of Directors, which can be, and often is, a single corporate director to whom the investment manager reports.

Because the investment is open ended, the price at any point will always reflect the net asset value of the underlying assets held.

Unlike unit trusts, OEICs typically have a single pricing structure, i.e. a single price at which shares are bought and sold and from which any initial or transaction costs and charges are deducted at the point of purchase and/or sale.

An OEIC manager will pursue a specific investment strategy, which may be 'active' (i.e. with an objective of outperforming a market benchmark) or 'passive' (i.e. with the objective of tracking a specific benchmark index). Underlying investments may be equities, bonds, property, commodities, or money market instruments. The investment objective of an OEIC may be orientated towards income, through distributions of interest or dividends, or capital growth. The policy of the investment manager may involve concentration on investment in a particular geographical market or in assets with a particular style or market capitalisation, or concentrated in a particular sector of the market.

OEICs were first introduced to the UK in the late 1990s and the structure has gained popularity over recent years with many existing funds and most new launches opting for the OEIC structure rather than the unit trust.

For more information on OEICs you can visit the Investment Management Association site at www.investmentuk.org

Offshore Bond

A product wrapper that takes advantage of the specific personal tax rules applicable to life policies.

A life bond does not distribute income by way of dividends or interest but the investor can generate an 'income' from regular encashment of units.

This facility is commonly used in tax deferral strategies, in particular taking advantage of the facility to withdraw up to 5% of the original capital without incurring immediate tax liability for up to 20 years.

Although the investor does not pay CGT on gains made within life funds, part or total encashments on offshore life funds may incur an income tax liability at the investors highest marginal income tax rate; a realised gain on a life fund may have the effect of 'pushing' an individual into the higher rate tax band. The tax calculation to determine the rate applicable to gains is carried out under what is known as 'top slicing' rules.

When deciding whether to invest in an offshore bond, the investor should consider the impact of the single CGT tax rate of 18%. Investors should also compare the advantages of the tax deferral opportunities offered by an offshore bond with the potential income tax liability on encashment, compared to the CGT regime that applies to other collective investments such as unit trusts and OEICs.

The investor should also consider the benefits of the offshore bond compared to the onshore alternative where internal taxation of income and gains applies but where gains are subject only to higher rate tax liability.

Novia offer an offshore bond provided by Royal London 360 Insurance Company Limited in the Isle of Man.

Open Ended

An investment fund with an open ended structure, such as a unit trust or OEIC, is able create and cancel further shares/units as investors buy and sell their stakes in the fund. This is usually directly with the investment manager.

As there is no fixed amount of shares/units in circulation, with the investment manager able to create or cancel, such an investment fund is known as open ended.

As such, the price of the shares/units is set by the investment manager based on the value of the underlying assets held by the fund. This is in contrast with closed ended investments such as investment trusts which issue a fixed amount of shares which trade based on supply and demand.

Optimisation

The process of arriving at the optimal asset allocation for an investment portfolio, given a specific risk profile and timeframe. This is typically achieved by performing an analysis of a series of return probabilities on a range of asset classes.

Technology has brought optimisation tools, previously the exclusive preserve of institutional investors, into the realm of retail investors and advisers.

Such tools enable advisers to carry out modelling exercises in order to identify the most suitable asset allocation, both strategically (broad asset classes such as cash bonds and equities) and tactically (narrower asset classes such as equity style, geography and bond yield). The optimisation process identifies where an investor's portfolio should be in relation to the mix of assets offering the potential for the best return given a certain level of risk. Having established the optimal asset allocation, securities that best achieve that target can then be selected.

Pound Cost Averaging

The principle of managing the timing risks associated with investing in stock markets by 'drip-feeding' regular investments into an asset or fund over a time period. This is rather than risking the investment of a lump sum at one specific date. Thereby, exposure to possibly volatile markets is 'managed' by gradually building up the investment over a period and effectively 'averaging out' the price at which the investment is acquired over time.

The perceived benefit of pound cost averaging is that the investor pursuing longer term growth can actually benefit from falling markets in the short term. Simply, when prices fall, each contribution buys more shares or units, thereby increasing the potential for growth when the price rises. Of course, if prices rise throughout the purchase period, then the opposite is true. However, in this context, it is important to remember than pound cost averaging is essentially a risk mitigation exercise.

Product Wrapper

A 'shelter' with certain characteristics placed around an investment portfolio, typically for tax purposes. This may be to take advantage of the particular tax features accompanying a particular product, like an ISA or pension. Novia product wrappers incorporate a Cash Facility to facilitate the movement of money and ensure transparent and efficient investment.

Common examples of product wrappers in the UK include:

- Investment Bonds, which take advantage of the specific tax rules applicable to life assurance policies. These are often used in tax deferral strategies, in particular taking advantage of the ability to withdraw up to 5% of the original capital without incurring an immediate tax liability for up to 20 years.
- Pension Schemes, such as a Self Invested Personal Pension (SIPP) which utilise the tax advantages of HMRC approved retirement savings schemes. Returns are exempt from personal taxation whilst accumulating the pension fund. However, at retirement, only up to 25% of the accumulated fund can be taken as tax free cash; the remaining fund must be used to provide an income which is taxable in payment under PAYE rules.
- Individual Savings Accounts (ISAs), either cash or stocks and shares.
- Novia also provides a General Investment Account which has no specific tax advantages but allows unlimited and unrestricted contributions and withdrawals.

Redemption Yield

The annualised rate of return on a bond (fixed interest security) or bond fund, expressed as a percentage, assuming that the asset is held to maturity.

Redemption yield reflects not only the interest payments a bondholder will receive, but also the gain or loss at maturity compared to the current price.

The income element is defined by calculating the current yield. The gain/loss element is calculated by taking the difference between the current market price and the face value of the bond at maturity.

Re-registration

The process of allowing investors to transfer investments, typically authorised funds such as unit trusts or OEICs, from one investment account or platform to another without the need for sale and purchase transactions.

Thereby, the investor will minimise transaction costs, avoid the risk of a period out of the market and also avoid any potentially disadvantageous tax implications of disposal and re-acquisition.

Also see in-specie transfer.

R-Squared

A statistical measure that reflects the percentage of an investment's price movements that can be explained by movements in a benchmark index.

R-squared values range from 0 to 100.

- An R-squared of 100 means that all movements of an investment are completely explained by movements in the index.
- A high R-squared (between 85 and 100) indicates the fund's performance patterns have been broadly in line with the index.
- A fund with a low R-squared (70 or less) doesn't act much like the index so that a comparison of the fund's behaviour with reference to index can become relatively meaningless.

For example, a higher R-squared value (at least 70) will indicate a more useful alpha and beta figure. A fund with an R-squared value close to 100 with a beta below 1 indicates that it is offering a high risk-adjusted return. Where the R-squared figure is low, the Alpha and Beta statistics should be ignored.

SEDOL Code

The Stock Exchange Daily Official List or SEDOL is the standard identification code for all securities trading on the LSE and other smaller stock exchanges in the UK.

A SEDOL code is made up of seven alphanumeric characters.

Self Invested Personal Pension (SIPP)

A retirement fund held under HMRC approved pension rules that enable investors to hold a broad and extensive range of investments within a tax-advantaged pension tax wrapper.

Although a SIPP is a form of personal pension the invested assets are held under trust by the SIPP provider for the benefit of the investor.

Eligible investments for a SIPP include:

- Particular stocks and shares quoted on a recognised UK or overseas stock exchange
- Government Securities (Gilts)
- Unit trusts and OEICs
- Investment trusts
- ETFs
- Insurance company funds
- Traded endowment policies

A SIPP can borrow up to 50% of the value of its assets.

As with all pension contracts, contributions attract tax relief at the individual's highest marginal tax rate and are subject to an annual limit of gross earnings up to a ceiling of £235,000 for the tax year 2008/9 and to a Lifetime Allowance of £1.65 million for the tax year 2008/9.

For more information see: www.pensionsadvisoryservice.org.uk

Sharpe Ratio

A risk-adjusted measure of fund performance developed by Professor William Sharpe.

Sharpe Ratio is a statistical measure of risk adjusted return and is calculated by dividing the annual excess return of a fund (the return in excess of the risk free rate, cash) by volatility as measured by the annual standard deviation of its benchmark.

Sharpe ratio should be positive, and higher ratios indicate superior risk-return characteristics. Negative Sharpe ratios are misleading and should not be used to compare the risk return characteristics of a fund.

SICAV

Societe d'investissement a capital variable: an open ended investment company structure similar to an OEIC in the UK and extensively used in Western Europe.

European compliance directives have meant that SICAVs (along with OEICS and other equivalently structured funds) are now increasingly marketed across Europe.

Single Pricing

A pricing structure where a single price applies to both the purchase and sale of an investment. Single pricing is the typical pricing structure of Open Ended Investment Companies (OEICs) and most individual securities.

The fund manager will create and sell units to investors but also buy and cancel units at the same price. Any upfront purchase or sale fees or charges are simply added to the single price to arrive at the overall transaction cost.

This is in contrast to dual pricing, which typically applies to unit trusts. Over recent years, the single priced OEIC structure has grown in popularity with fund managers and investors, not least because it is compatible with standard practice in other European markets.

Standard Deviation

A statistical measure of variability, i.e. the degree by an individual value may vary from an average or defined data.

In investment terms, standard deviation is used to analyse risk by looking statistically at the range of possible returns that could be achieved from an investment or portfolio. A high standard deviation suggests a high degree of potential volatility and therefore a riskier investment; a low standard deviation suggests the opposite.

Stock Exchange

A Stock Exchange is the market on which negotiable securities such as shares and bonds are traded.

The LSE is one of the largest and longest established exchanges in the world and its history can be traced back more than 300 years to the Coffee Houses of the late 17th century.

Milestones in its history include the formation of the first regulated exchange in 1801, admission of women to membership for the first time in 1973, and the de-regulation, known as the ‘Big Bang’ in 1986.

For more information on the LSE you can visit www.londonstockexchange.com

Structured Product

A wide range of investment offerings with no single identifying feature but which can generically be defined as 'bespoke' investment vehicles which may be individually designed or created as a mass market, retail product.

Although the products vary widely, they tend to be characterised by a combination of capital protection or underlying guarantee with the potential for a higher return through exposure to a higher risk vehicle.

It is essential that the would-be investor reads and fully understands the (sometimes complex) terms and conditions to understand fully the potential risks and returns on offer.

Total Expense Ratio

A percentage figure that is indicative of the proportion of a fund's assets consumed by all the annual costs it incurs.

The Total Expense Ratio (TER) provides a more accurate and robust picture of the overall cost of managing the investor's money than the more commonly quoted Annual Management Charge.

However, it is important to note that even the TER does not capture the entire costs of a fund:

- it excludes the (admittedly highly variable) initial charges
- it does not take into account broking/dealing costs or the potential impact of 'market costs', (especially for a larger fund, the impact that its trading in a particular share or bond might have on the price of that security).

Reduction in Yield (RIY) figures can be used instead of TERs (and these are also used in tables which compare investments). RIY is similar to TER, but the latter is more widely accepted globally and does not attempt to include the problematic initial management charges.

Tracking Error

Defines the volatility of the variations in returns between a fund and its benchmark. Tracking error is also commonly known as 'Active Risk'.

Tracking Error considers the historic correlations and variances of risk factors and is calculated as the standard deviation of the relative monthly or quarterly returns of the fund and benchmark.

It is expressed in terms of the expected size, in percentage points, of each standard deviation of return.

It can indicate how effectively a fund is tracking its benchmark and what degree of 'active risk' an investment manager is taking to achieve returns: the higher the tracking error, the greater the degree of risk.

TVAS – See CETV/CEV

Unit Trust

An open ended collective investment vehicle, enabling an investor to manage risk through investment diversification and the professional day to day management of a portfolio of assets.

A unit trust is established under trust law and is run by a Board of Trustees to whom the fund manager reports.

Because the fund is open ended, the price at any point will always reflect the underlying net asset values of the underlying assets.

Unit trusts typically have a dual pricing structure, i.e. an offer or purchase price, and a lower bid or selling price. The difference between the two prices reflects the initial cost of investing.

Unit trust managers will pursue a specific investment strategy, which may be 'active' (i.e. with an objective of outperforming a market benchmark) or 'passive' (i.e. with the objective of tracking a specific benchmark index). Underlying investments may be equities, bonds, property, commodities, or money market instruments. The investment objective of a unit trust may be orientated towards income, through distributions of interest or dividends, or capital growth. The investment policy of the manager may involve concentration on investment in a particular geographical market or in assets displaying a particular style or market capitalisation, or concentrated in a particular sector of the market.

The popularity of the unit trust structure has waned over recent years with many existing funds and most new launches opting for the OEIC structure. This is seen to be more compatible with pan European markets and allows the manager to market a fund

across the EU provided the fund complies with certain regulations.
For more information on unit trusts you can visit the Investment Management Association site at www.investmentuk.org

Volatility

Volatility is a measure of the range or degree to which the price or value of an investment could change over a specified time period.

In investment terms, this is defined as the standard deviation of price changes of the continuously compounded returns of an investment over a specified time period. Technically this is also described as 'historical volatility' because it captures volatility based on a statistical analysis of historical returns.

Wealth Management

Wealth management is a broad definition that encompasses many different approaches and providers. Typically, wealth management looks at the strategic management of a client's wealth, i.e. assets and (sometimes) liabilities. In the UK there is a broad range of professional advisory firms who are authorised and regulated by the Financial Conduct Authority, providing a 'regulated activity', i.e. the provision of investment advice.

A wealth management strategy will usually involve:

- setting investment goals and timescale(s) driven by client aspirations, expected and unexpected life events
- establishing priorities
- analysing current and potential future capital and income resources, assessing the individual's appetite for risk
- agreeing a suitable mix of assets, or asset allocation as it is known, based on all of the above
- identifying appropriate tax efficient products and investments to maximise the prospects of achieving the goals
- tax planning and inheritance issues.

Professional wealth management strategies will take a long term view whilst reflecting shorter term needs. Regular monitoring and review in the light of changing needs and/or market conditions are essential.

Wealth management strategies will typically be actively managed, in some cases on a discretionary basis where an adviser or discretionary manager will take investment decisions on a client's behalf.

A successful approach to wealth management will use resources available to the adviser, such as the ability to transact in a timely and cost efficient manner and the use modelling techniques and planning tools.

Wrapper - see product wrapper

Queen Square House
Queen Square Place
Bath
BA1 2LL
Telephone: 01225 437600
Fax: 01225 437601

Blackwell House
Guildhall Yard
London
EC2V 5AE
Telephone: 020 7556 1000

Edmund House
12 – 22 Newhall Street
Birmingham
B3 3AS
Telephone: 0121 214 1525

Email: info@beckfordjames.com
www.beckfordjames.com

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