

Can redundancy boost my income in retirement?



Lucy Warwick-Ching Wealth Questions

I am taking voluntary redundancy and expect to get around £130,000, £30,00 of which will be tax-free. I am also taking a 25 per cent tax-free lump sum of £100,000 from my final-salary pension fund and will start drawing an annual income of around £30,000 from the scheme.

I am a 62-year-old man with two sons who will inherit my house one day, but I would like to use my redundancy money and the tax-free pension cash to

help generate extra retirement income. I have around £5,000 in other savings and some credit card debt.

I would like to generate as much income as I can, but have no idea which institutions pay a good rate of interest. I also want to be as tax-efficient as possible. I am not interested in taking much, if any, risk with my money.

Jonathan Fry, private wealth director at Jonathan Fry & Co, says that although, by taking voluntary redundancy, you are retiring a few years earlier than you might have expected, this blow is softened significantly by your final-salary pension. It will provide an income of £30,000 a year (presumably with some measure of inflation protection) and a tax-free lump sum of £100,000.

Final-salary schemes are now the exception rather than the rule for many

younger employees and you are in a much better position than many entering retirement.

A key question for you is whether the income from your final-salary pension of £30,000 a year is sufficient, after tax, to cover your expenditure, or whether you need to generate further income from your capital. It is not unusual for those who retire early to spend more significant amounts on travel and leisure while still in good health. You will, of course, also be entitled to a state pension when you are 65, which will provide an additional source of further income.

For the time being, you say you wish to generate as much income as you can while investing as tax-efficiently as possible. Importantly, you also say you don't wish to take much, if any, risk. This is a fundamental dichotomy that many investors face and the simple fact is that

higher returns can only be provided by accepting greater risk.

So investors have two choices: to leave their capital in cash deposits which do not fluctuate in value, but offer little protection against inflation; or to accept volatility as the price of protecting the real value of capital over the longer term. Investing in real assets, such as equity and property, has traditionally been the best

YOUR QUESTIONS

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way of protecting the real value of capital, but the last decade in equity markets has been hugely challenging for the majority of private investors.

My advice is generally to focus on matching the asset classes in which you are investing with your

likely needs. If you want a very high level of disposable income in the earlier years of your retirement then you may be better advised to keep a relatively high cash balance and spend some of your capital. This would be a more realistic alternative for those wishing to adopt a cautious approach than investing in volatile investments in the hope of achieving a higher rate of return.

The average return on the top three instant accounts we recommend via our cash management service is 3.08 per cent for personal, instant-access accounts. This rate increases to 4.02 per cent for accounts with a 24-month term.

Should you be willing to take a little more risk with some of your capital, I would recommend you first utilise your individual savings allowance (Isa) of £10,680 for 2011/12. No tax is payable on capital gains

arising on investments and no further tax is payable on the income received from Isa savings and investments.

You could also use your Isa allowance for 2012/2013 and possibly for further years down the line, depending upon the balance you wish to retain in cash.

I would recommend a diversified fund portfolio, with a relatively cautious attitude to risk. You might consider including Invesco Perpetual High Income, currently yielding about 4 per cent and run by Neil Woodford, which is defensively positioned, being predominantly invested in high-yielding blue-chip companies.

In addition, you could consider investing in the M&G Strategic Corporate Bond fund, which also yields about 4 per cent and invests predominantly in high-quality corporate bonds.