

## MONEY

FISCAL CARROT  
HOW RUNNING OUT OF  
CASH INSPIRED HISTORIAN  
NIALL FERGUSON P13

## Prosper in a low-rate world

How should families deal with the prospect of more interest-rate cuts in December? Niall Brady turns to the experts for advice

ECONOMISTS are predicting that interest rates could fall as low as 2% as the European Central Bank (ECB) seeks to stave off a prolonged recession.

The ECB has cut rates twice since the beginning of October, bringing them to 3.25%, their lowest level in two years. Simon Barry, a senior economist at Ulster Bank, predicts more reductions before Christmas.

"We expect another half-point cut at the ECB's December meeting, and rates look destined to get to 2% next year, if not even lower," he said. "Since the ECB was formed in 1999, it has never cut rates by so much so quickly."

Falling rates are bad news for savers. Banks and building societies began to scrap many of their top deposits last week and the headaches for savers will intensify from January, when the government raises deposit interest retention tax (Dirt) from 20% to 23%.

We look at how households can manage their finances in a world of low interest rates.

## Savers

Fixed-rate bonds are a good way for savers to protect their money as interest rates slide. Some of the best deals disappeared last week, though, after the ECB's latest cut. Rates on bonds still available are closer to 5%, leaving savers struggling to keep pace with inflation after Dirt has been deducted.

Irish Nationwide, which led the market for much of the year, used to pay 6% interest fixed for six, nine or 12 months. It will slash the rate to 5.25%, fixed for three or six months, from tomorrow. Those willing to lock up their money for longer with the building society can get 11% fixed for two years.

Bank of Scotland used to pay 6.25% fixed for six months or 6% fixed for three, but only on deposits larger than €100,000. Now it offers 5.5% for six months or 5.25% for three.

First Active has bucked the trend, though, launching an account last week that pays 6.25% fixed for six months on deposits of €20,000 to €3m.

Peter Kinahan, editor of Mycash.ie, a price comparison website, said: "Many of the recent offers were not sustainable, despite the banks' pressing need for savers' funds. There may be a relatively short window left to take advantage of some of the better offers still available."

## Investors

Gilts, which are bonds issued by the government to finance the national debt, tend to perform well when interest rates fall because their fixed income looks more attractive in a low-rate world. The government is also being forced to pay a better rate when it issues new gilts, reflect-

ing the tarnishing of Ireland's creditworthiness by the state's €440 billion bank guarantee scheme.

However, advisers warn that savers would be better off sticking to deposits. Brian Weber, head of the Dublin office of wealth adviser Citi Quilter, said: "Gilt yields have crept up a bit however you'd earn more on a 12-month fixed deposit. Income from gilts is taxed at the marginal rate — 41% for most people — which doesn't compare favourably with Dirt tax on deposit interest."

Corporate bonds are a better alternative, although they are riskier than gilts as companies are more likely than governments to default on their debts. The increased risk has widened the yield gap between gilts and corporate bonds to a 50-year record in America.

Niall Tinney, a partner at Bloxham stockbrokers, said: "Investors require a higher yield on corporate debt because there is a greater chance of default during a recession."

Those willing to take the risk should invest through funds rather than buying bonds directly. "A fund is likely to give a better balance of return and risk. You may pick up a better coupon by investing directly but you'll lose most of it in tax because the coupon will be taxed at your marginal rate, just like gilts," said Weber.

"If you invest through a bond fund, though, you're liable only for an exit tax, which is 26% from next January."

Savers looking for better returns have traditionally invested in bank shares, as the dividends paid tended to be higher than the returns given to depositors, especially when interest rates fell. Bank of Ireland and Irish Life & Permanent have stopped paying dividends, while Allied Irish Banks (AIB) will not make cash distributions to shareholders.

Investors can still earn healthy returns in other sectors, however. "Decent blue-chip stocks that pay safe dividends will be worth looking at in five or six months' time," said Weber. "Many companies have low borrowings as they head into the recession, so their dividends should be relatively safe."

Bloxham has dumped most banks from its High Yield equity fund, which now yields about 5%. The fund lost 2.2% of its value between July and September, considerably less than the average managed fund, which shed 9.5% as stock markets plummeted.

Its largest holdings include BP, Roche and Johnson & Johnson. "These stocks are not immune from the downturn, but they're the type of cash-rich, profitable companies that will benefit most when money starts coming back to the stock market," said Tinney.



Crotty uses an account comparison website to ensure he gets the best interest rates for his savings without having to lock them in for more than three months

## Borrowers

Homeowners who have tracker mortgages are the only borrowers who can be sure that their repayments will fall in line with interest rates because their loans are pegged to the ECB rate. Lenders have agreed to share the last two interest-rate cuts with those on standard variable mortgages, although they may be less generous with future interest-rate cuts.

Those most likely to lose out are borrowers on newer loan-to-value variable rates from lenders such as

Bank of Ireland, Permanent TSB and KBC Homeloans, because they have already held back some of the recent rate reductions.

Mortgage experts advise those affected to consider switching to lenders with low standard variable rates or to take advantage of the low-rate environment to fix their rates for the long term.

Karl Deeter, operations manager at Irish Mortgage Brokers, said: "All the good trackers have gone, so the options are a good standard variable rate — AIB's is 5% and due

to fall to 4.5% — or fixing for the longer term, if you can find a good rate to lock into."

AIB and EBS have 10-year fixes at 5.65%, while Haven charges 5.66%. Ulster Bank has the best unrestricted deal on five-year fixes, at 5.1%. National Irish Bank will do the same mortgage for 4.76% — but only for those with at least 50% equity in their homes.

Deeter advises those thinking about fixing to wait until the new year, when he expects better deals to become available. "People have shied away from long-term fixes, but they could pay off if all the money that governments are pumping into the world economy to stave off recession leads to hyperinflation and therefore to higher interest rates," he said.

## Approaching retirement

Advisers are recommending that retirees fix their annuity rates now, after hefty rate cuts in recent months and the prospect of more to come caused annuity rates to slide. Payouts from Irish Life have dropped by €1,500 since the summer to €17,250 a year for a 65-year-old male with a €250,000 pension pot, according to Richard Morton of Moneywise, a pension adviser.

## Liquid assets keep options open

One investor says cash is the best way to prepare for opportunities, provided you monitor bank rates

INTEREST rates are on the way down but John Crotty, 44, plans to keep a large chunk of his money in cash.

"I'm inclined to take a reasonably conservative view, keeping 40%-50% of my money liquid," he said. "Keeping a large position in cash means you're ready to strike when the right investment opportunity arises, be it in stocks, shares or property."

Earning a consistently good rate of interest can be tricky, though, with banks and building societies seeking to pull in savers with eye-catching offers that last only for a short time.

Crotty, a partner in the insurance brokers Lennon Earley Crotty, of Dublin, uses a savings comparison website, IrishDeposits.ie, to track rates. It identifies the best deposit accounts and contacts clients when their savings are about to mature, warning them that they could lose out if they fail to move their money elsewhere. "Unless you keep an eye on the deposit market, the rate paid on

your savings can decrease without the bank bringing it to your attention," said Crotty. "When a rate expires, the site makes sure you're still maximising the return on your savings, even if that means staying with the same bank but switching to a different account."

He used the website, which is free, to find a new home for his savings three months ago, moving to an instant-access account at Bank of Scotland that pays 0.5% more interest than his old bank.

Even though banks tend to keep their top rates for long-term savers, Crotty is reluctant to tie up his money. "I'm not inclined to lock in for more than three months," he said.

The stock market is starting to look attractive, with many blue-chip stocks knocked down to bargain valuations. "If you're prepared to take a long-term view — three to five years, say — this could be a very good time to start buying equities again," he said. "The way share prices have gone in recent months, you probably couldn't go too far wrong if you stick with good-quality companies."

Niall Brady

## TOP FIXED-RATE SAVINGS

	Rate	Term	Minimum
First Active	6.34%	6 months	€20,000
Anglo Irish Bank	6.00%	12 months	€1,000
Halifax	5.90%	12 months	€2,500
EBS	5.60%	12 months	€20,000
National Irish Bank	5.52%	6 months	€5,000
Irish Nationwide	5.25%	12 months	€20,000
Northern Rock	5.00%	12 months	€1,000
Bank of Ireland	5.00%	12 months	€10,000

Source: The Sunday Times

## When was it ever 'normal' for homes to 'earn' more than jobs?

JILL KERBY  
COMMENT

When do you think things will get back to normal, ask people seeking reassurance that it was "normal" for their homes to "earn" more money than they did by going to the office or factory every day.

They're asking the wrong person if reassurance is what they want. I'm working on the assumption that things are only going to get much, much worse in the coming months and years as a result of the compounding of the credit and debt mistakes that have already destroyed the banking system. You may have noticed already that no

amount of loans, credit facilities, lower interest rates and stimulus packages has so far "normalised" the global banking sector, kick-started lending or stimulated stock markets. I can't see this changing, not even with The One in office in the White House.

The bailouts have been so ineffective that the US president-elect seems determined to try a different tack by handing money directly to America's bankrupt industries — like the Detroit automakers — and struggling mortgage holders. Good luck to him, especially since he has also promised to lower taxes for all but the top 5% of American earners,

slash interest rates further and increase spending on education, healthcare, alternative energy programmes and social welfare entitlements.

I have a much more modest plan in mind. Since my pooled pension funds have taken such a hammering, and I'm still being charged outrageous fees, I've started committing my cash to a little investment ark of my own. I'm looking at global — mainly American companies — that are trading at their lowest prices for years but are still paying strong dividends and have huge cash moats — companies like Microsoft, Intel, Walmart, Tesco, McDonald's, Exxon and British Petroleum, Gillette, Colgate-Palmolive, Coca-Cola and Johnson & Johnson.

With hyperinflation inevitable, I want some more gold and silver. The trouble is that physical gold is selling at a huge premium, while the counterparty risk for exchange-traded funds, a backdoor into precious metals, is too high. That's why I'm willing to risk some money by adding a couple of junior gold and silver mining companies. I've been reading about companies whose share prices are selling far below their pools of cash, companies such as Silver Bear Resources and ATW Gold Corp, or perhaps a low-cost fund of gold-mining shares.

Food commodities, timber, water and energy shares have all dropped in price, but their prospects look better than the financial and consumer shares that

dominated indices before the crash this year.

The only stimulus package I'm counting on this year is the one I put together myself.

## Permanent's temporary solution

Getting workers effectively to make themselves redundant is an innovative answer to the problem of how companies can reduce their payrolls with as little industrial disruption as possible.

When you think about it, Permanent TSB's proposed sabbatical scheme should be a hands-down winner, given the bank's success over the years in convincing young borrowers in particular to take out expensive loans that were not in their best interest.

That's not to say that Permanent TSB's two-year and three-year sabbatical offer to its staff isn't without merit for the person who doesn't have serious financial commitments, or who already had a plan in mind involving travel or further education but has no access to funding.

How often does someone come along and offer you between €20,000 and €35,000 if you agree to make yourself scarce for a few years, and then sweetens the pot further by promising your job back if you decide to return?

Ideally, Permanent TSB would prefer to get rid of a layer of unionised middle managers in their forties and fifties who

are costing the bank a fortune in salary and benefits at a time when there is little business being generated. Because such employees are unlikely to be able to afford a mid-life gap year or two, they had little choice but to target the under-30s.

The bank is undoubtedly counting on a fair proportion of its out-of-sight, out-of-mind workers never bothering to return at the end of their two or three years. Its goal is to be considerably leaner and lighter by then and remain so. But even this group might want to ensure that a final redundancy settlement is part of any sabbatical agreement they sign.

On another practical note, anyone who takes up this plan might also want to crunch a few numbers before they temporarily sign their job away: their sabbatical payment will still be treated as income, although it probably won't attract much tax, if any. Nevertheless, it won't stretch that far if you still have to use it to pay off a student loan, car loan or credit card debt.

Time will tell, but this little sabbatical scheme could even end up as a template for a short-term but entirely voluntary cutting of the bloated civil service payroll.

With a chorus of economists and opposition politicians now calling for an immediate 10% cut in civil service pay, the alternative — to facilitate thousands of young clerical officers to take a sabbatical in Australia or America — could be as tempting to Brian Cowen and

Brian Lenihan as it was to the bosses at Permanent TSB and Irish Life.

## Haggle, now that cash is king

The dining room-cum-office-cum-junk room in our house is undergoing a transformation into a proper study and office, where the television and computer gaming will be banned.

The room needs a sofa. The furniture discount shops on Long Mile Road, Dublin, need customers. That is why, when I told the salesman that I had a maximum of €800 to spend, but the sofa I really wanted was €1,056 — already reduced from €1,700 — he instantly said he'd take my offer if I paid him cold, hard cash.

Meet "haggle" the twin sister of "thrift". Clearly, neither of us is very experienced at this game. If his shop had been in the Hammamet souk that I visited on holiday a couple of years ago in Tunisia, or even in Rome where the price you see is not the price the locals ever pay, I would have opened with an even lower offer and he would have sealed the deal with a much higher price.

I expect we're both going to get better at haggling as this recession grows, but in the meantime I intend to start working on my technique with the rest of my Christmas shopping.

In the land of the clapped-out credit card, cash isn't just a king. He's an emperor.