Pennymatters
THE MODERN APPROACH TO FINANCIAL ADVICE

Pennymatters Ltd
Building 329, Doncastle Road
Bracknell, Berkshire RG12 8PE
T: 01344 988390 F: 01344 988394
E: enquiries@pennymatters.co.uk
W: www.pennymatters.co.uk

A timely proposition

Considering gilts for your investment portfolio?

High interest rates make gilts an attractive option for some investors, especially higher rate taxpayers who benefit from the tax exemption from capital gains. What exactly are gilts? These UK government bonds, or debt securities, are issued to finance public expenditure. Their appeal lies in their low-risk nature and guaranteed income.

SECURING SAFE INVESTMENTS WITH GILTS

Gilts are considered one of the safest investment options because the British government fully backs them. Think of a gilt as an IOU from the Treasury. Investors receive regular interest payments in return for lending money to the UK government. Most gilts offer a fixed cash payment (or a coupon) every six months until maturity, when the final coupon payment is made along with the return on the original investment.

TRADING AND MATURITY OF GILTS

Investors have two options: hold on to the gilts until maturity or sell them on the secondary market, much like company shares. Short-term gilts mature between one to five years, medium-term gilts have a lifespan of five to fifteen years, while long-term gilts exceed fifteen years, some even extending up to fifty years. Generally, gilts with longer lifespans have higher interest rates than those maturing soon.

UNDERSTANDING GILT YIELDS

The annual return an investor gets for holding a gilt over the next 12 months is known as the yield. It's calculated by dividing the annual coupon payments by the current market price. Various factors influence gilt yields, including the outlook for interest rates, inflation and market demand for gilts. Interestingly, bond prices and yields move in opposite directions.

THE RISE OF GILT YIELDS

Since the pandemic, interest rates have skyrocketed as the Bank of England tries to control inflation. Interest rate changes significantly impact bond prices, especially when they are forecasted to keep increasing. As interest rates increase, bond prices generally fall, and vice versa. This inverse relationship is due to new bonds with high coupon rates being issued at higher interest rates than older bonds that have been issued at lower rates.

THE TAX BENEFITS OF GILTS

While Income Tax applies to the interest earned from gilts, they are entirely exempt from Capital Gains Tax (CGT). This means there's no CGT to pay on any profits from selling a gilt or when it matures. This exemption is especially beneficial for higher rate taxpayers who'd otherwise have to pay a 20% CGT. Moreover, there's no tax on gilts held in a tax-efficient wrapper like an Individual Savings Account (ISA) or a Self-Invested Personal Pension (SIPP).

PROTECTING CAPITAL WITH INFLATION-LINKED GILTS

For investors concerned about inflation, inflation-linked gilts offer a reliable way to protect their capital if held to maturity. The principal and interest are tied to inflation, ensuring investors receive a return that keeps pace with the cost of living.

GILTS AND PORTFOLIO DIVERSIFICATION

Gilts provide a safer alternative during uncertain times, and their low correlation with stock markets makes them an alternative diversifier. By including gilts in a diversified portfolio, investors can mitigate risk and balance their exposure to different asset classes as the coupon is fixed at the outset. ■

ARE YOU LOOKING TO MAKE BETTER-INFORMED INVESTMENT DECISIONS?

Don't hesitate to get in touch for further information or advice on adding gilts to your portfolio. We're here to help you make informed investment decisions. To find out more, contact us – we look forward to hearing from you.

THIS ARTICLE DOES NOT CONSTITUTE TAX OR LEGAL ADVICE AND SHOULD NOT BE RELIED UPON AS SUCH. TAX TREATMENT DEPENDS ON THE INDIVIDUAL CIRCUMSTANCES OF EACH CLIENT AND MAY BE SUBJECT TO CHANGE IN THE FUTURE. FOR GUIDANCE, SEEK PROFESSIONAL ADVICE.

THE VALUE OF YOUR INVESTMENTS (AND ANY INCOME FROM THEM) CAN GO DOWN AS WELL AS UP, WHICH WOULD HAVE AN IMPACT ON THE LEVEL OF PENSION BENEFITS AVAILABLE.