A Guide to
INVESTING FOR INCOME

Selecting the right type of investments for your future

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Welcome

Welcome to 'A Guide to Investing for Income'. Generating an income from your investments will be an important requirement especially if you've retired or are approaching retirement, or if you need to supplement your salary, or have a relatively short investment timeframe.

Income seekers in recent years have experienced frozen interest rates at historic lows which have resulted in real losses for many savers in bank and building society deposits which have failed to match inflation.

PLEASE NOTE THAT THIS IS A GENERAL GUIDE DESIGNED TO HELP YOU THINK ABOUT YOUR INVESTMENT NEEDS. IT DOES NOT PROVIDE SPECIFIC ADVICE. IF YOU ARE UNSURE OF YOUR FINANCIAL POSITION OR ABOUT WHICH TYPE OF INVESTMENT IS RIGHT FOR YOU, PLEASE CONTACT US FOR FURTHER INFORMATION.

FIXED INTEREST

The most popular forms of income investment are bonds (which are also known as 'fixed interest' investments) and cash, both of which pay a regular, consistent rate of interest either annually, twice a year or four times a year. You can also obtain an income from shares in the form of dividends, and many equity funds are set up solely with the aim of generating a stable income. Importantly equity income funds often aim to achieve not only stability, but an increasing income in the long term.

GOOD CASH FLOW

Income stocks are most usually found in solid industries with established companies that generate good cash flow. They have little need to reinvest their profits to help grow the business or fund research and development of new products and are therefore able to pay sizeable dividends back to their investors. Examples of traditional income-generating companies would include utilities such as oil and gas, telephone companies, banks and insurance companies.

You should remember that these investments do not include the same security of capital which is afforded with a deposit account.

10 INCOME INVESTING TIPS

1. SUSTAINABLE LONG-TERM DIVIDEND GROWTH
Investing in businesses when the growth potential is not reflected in the valuation of their shares not only reduces the risk of losing money, it increases the upside opportunity.

2. INFLATION MATTERS
Always bear in mind the detrimental effect of inflation. Corporate and Government bonds offer higher yields than cash but returns can be eroded by inflation. Investment in property or equities provides a vehicle to help achieve an income that rises to keep pace with inflation.

3. CONSIDER INTERNATIONAL DIVERSIFICATION
A small number of UK companies account for some 40 per cent of UK dividend payouts. This compares with over 100 companies in the US, for example, that provide the opportunity to increase the longevity of dividend growth.

4. PATIENCE IS A VIRTUE
Investing for income is all about the compounding of returns for the long term. As a general rule, those businesses best placed to offer this demonstrate consistent returns on invested capital and visible earnings streams.

5. RELIABILITY IS THE KEY
Select sectors of the equity market that do not depend on strong economic growth to deliver attractive returns to investors.

6. HIGH AND GROWING FREE CASH FLOW
Look for companies with money left over after all capital expenditure, as this is the stream out of which rising dividends are paid. The larger the free cash flow relative to the dividend payout the better.

7. DIVIDEND GROWTH
In the short term, share prices are buffeted by all sorts of influences, but over longer time periods fundamentals have the opportunity to shine through. Dividend growth is the key determinant of long-term share price movements – the rest is sentiment.

8. CAUTIOUS APPROACH
Profits and dividends of utility companies are at the whim of the regulator. Be cautious of companies that pay a high dividend because they have gone ex-growth – such a position is not usually sustainable indefinitely.

9. INVESTMENT DIVERSIFICATION
The first rule of investment is often said to be 'spread risk'. Diminishing risk is particularly important for income-seekers who cannot afford to lose capital.

10. TAX-EFFICIENCY
Increase your net income by using an ISA (Individual Savings Account). ISA income is free of taxation, thereby potentially improving the amount of income you actually receive. ISAs are also free from capital gains tax, allowing you to switch funds or cash in without a tax charge.

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