Is it time to start using your 'Rainy Day' fund?

In these unprecedented times, financial planning could not be more important, even though it is quite clear that for many people, any plans that have been put in place may have to be amended.

For some, retirement may get pushed back, or new projects may get shelved. Yet, for others, these changing times may offer an opportunity, either as we manage the Lockdown procedures or once we come out of the crisis. What is most important is that your financial plan is flexible and fluid and able to change as the circumstances change.

In nearly all instances, we recognise that plans may have been thrown off course somewhat by the pandemic and highlights the issue we all have with any sort of plan. Basically, things change. As a famous boxer once said, "Everyone has a plan until they get punched in the face."

What is important in these instances is not the plans themselves, but the ongoing process of planning. A good example of that concerns one of the fundamentals of nearly all financial plans; the requirement for an emergency cash fund.

As ever, we are here to provide advice. Therefore, if you would like to discuss your current financial planning arrangements in light of any of the comments raised in this article, please do not hesitate to contact us.

This is money that is generally made up of three to six months income, often sat in a deposit based account.

People have different names for this account. Sometimes, it will be called an emergency fund, others refer to it as a 'rainy day' account.

Whilst the situation we are in at present may not feel like an 'emergency' as such, it can undoubtedly be referred to as a 'rainy day'. If we recognise this to be the case, then perhaps you should be considering drawing on this asset in these times.

Here are five reasons why we think you should look closely at your cash holding at present:

1) Take the pressure off your ongoing income

Whether you are working or retired, whether you have been furloughed, are self employed or work as a Company Director, this is a difficult time for everybody. Your income may be provided by employment or you could be drawing income from assets, but whichever it is, your circumstances will have changed and this may be a good time to consider your income requirements. We have already established that this is unquestionably a 'rainy day', so surely this asset must be considered. If you are not going to use this fund now, quite when would you use it? There will be plenty of time to build the fund back up again, when the sun shines as it were, so why not take some pressure off your regular income a little?

2) Interest Rates are historically low

When Bank Base Rates are historically low, this generally leads to lower savings rates. The Bank of England reduced their Base Rate twice in March and as at 1st June, it was just 0.1%, the lowest it has ever been. Should this filter down as expected, it will once again highlight how Cash offers little value in terms of an investment asset. Therefore, this may be a good time to make use of the asset.

3) Losing money in real terms

In April 2020, the retail price index dropped to just 1.5%. Whilst this is an historically low level in comparison to recent years, it is still higher than many deposit based accounts. The implication of that is crucial. When inflation runs at a higher rate than your cash account, it means that the money held in these savings accounts is losing money in real terms. This is also very important if you hold cash assets in excess of six months income. Due to the low interest rates being offered at present, cash is definitely not 'king' at present, and it may be a good time to consider whether this is the right place for those assets in the long term?

4) Take the pressure off your investments

If you are still continuing to take income from invested assets such a pension or ISA, it may be wise to slow that income down and supplement this income with your deposit based assets such as savings or Premium Bonds. Your Investment portfolio is very volatile at present and trying to draw income from it at the same time can put pressure on these assets as they are trying to recover. This is a difficult time for most investment portfolios and whilst we remain committed to a long term, multi asset, risk rated investment proposition, anything you can do to ease the pressure on those assets at present will help them in the long term.

5) Reduce the value of your estate

Cash assets in UK based savings accounts will form part of your estate for Inheritance Tax (IHT) purposes. Therefore, if you choose to spend some of this money rather than maintain its current level, not only will you benefit from some of the issues raised above, but you will also reduce the size of your estate for the purposes of an IHT calculation. For some people, this may be very important, potentially saving up to 40% in tax on death.

We recognise the importance of the 'rainy day' fund, and at times like this it has proved useful to many of our clients. However, do consider how much cash you have at present. This may be a good time to draw on that asset, for reasons suggested above. There will be time to build back the emergency fund when the 'sun shines'.