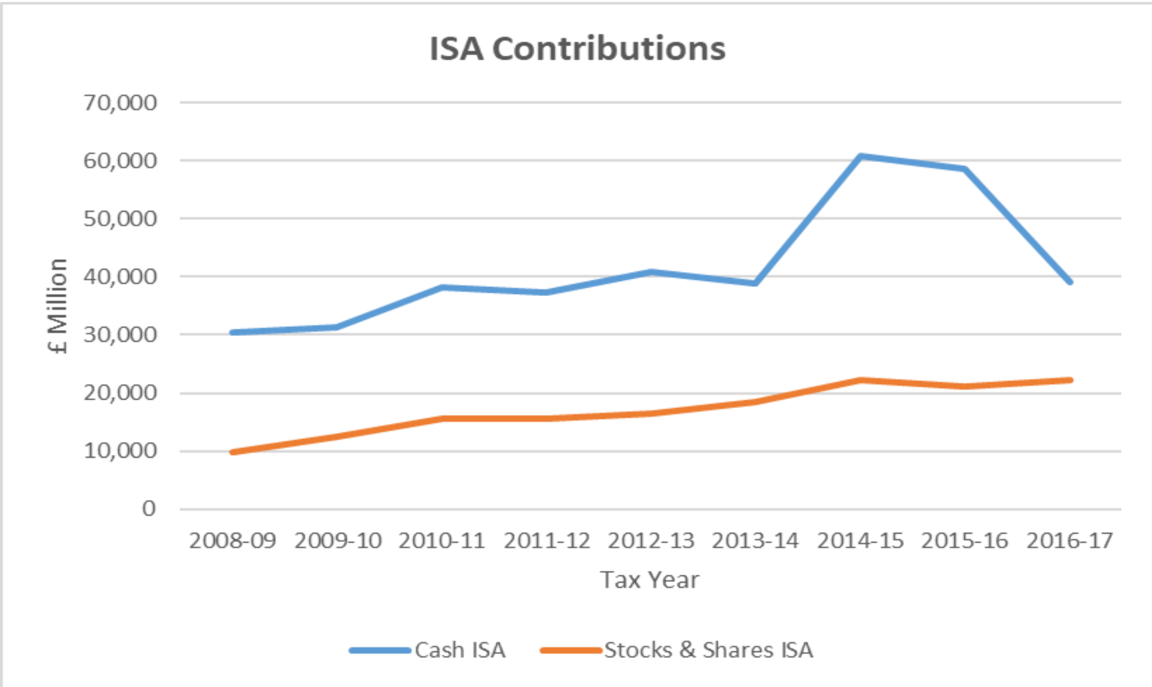
Cash ISAs losing favour

New statistics from HM Revenue & Customs (HMRC) show that cash withdrawals from individual savings accounts (ISAs) are probably more than matching fresh contributions.

In the world of ISAs, cash ISAs have long attracted more contributions than their stocks and shares counterpart. However, the pattern has started to change, as the graph below shows.



Source: HMRC

In the last tax year, contributions to cash ISAs fell by a third according to the latest HMRC data. They still amounted to over £39 billion, but the total held in cash ISAs increased by just £1.26 billion between April 2016 and April 2017. Once a year's interest is allowed for, even at current miniscule rates, that suggests more money was withdrawn from existing ISAs than flowed in through new contributions.

There are some good reasons why cash ISAs are going out of favour:

- ISA interest rates have been low for some years. The top rates for instant access are just over 1.0%, while the best *five year* fixed term rate is 2.15%. Neither compares well with inflation, currently at 2.9% on the CPI yardstick and 3.9%, as measured by the RPI.

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- The introduction of the personal savings allowance (PSA) in 2016/17 has meant that many people have no tax to pay on the interest they earn from non-ISA accounts. If you are a basic rate taxpayer, £1,000 of interest is tax free, while if you pay tax at 40%, £500 of interest suffers no tax. If you are an additional rate taxpayer, you do not receive a PSA.

- For wealthier investors, the reforms to dividend taxation – and the likely reduction in the dividend allowance from £5,000 to £2,000 next April – has made the tax shelter offered for dividends by stocks and shares ISAs relatively more attractive.

If you hold money in cash ISAs, it may make sense to review whether you should continue to do so. You could find yourself earning more interest outside an ISA or gaining more tax benefits from a stocks and shares ISA. For a discussion on your options, please talk to us.

The value of your investment can go down as well as up and you may not get back the full amount you invested. Past performance is not a reliable indicator of future performance. Investing in shares should be regarded as a long-term investment and should fit in with your overall attitude to risk and financial circumstances. The value of tax reliefs depends on your individual circumstances. Tax laws can change. The Financial Conduct Authority does not regulate tax advice.