Cost of Living

Why having an emergency fund matters and where to hold extra cash reserves

Having ready cash on hand is an essential part of any successful financial plan. When investing, it's important to hold an emergency fund. This readily available cash will mean you're prepared to protect yourself against the unexpected and also plays a vital role in maintaining your financial well being.

It's generally advised to keep between three and six months of household expenditure in an easy access account – more if you work in a particularly volatile sector.

If you're approaching retirement, you may want to keep even more of your wealth in cash.

An emergency fund and a retirement 'buffer' are only two aspects of how to think about cash – it can also be integral to a diversified portfolio. Cash tends to be the asset with the least associated risk. While cash offers the benefit of easy access, it also tends to provide lower long-term returns than other asset classes.

Over time, cash values can be eroded by inflation. So, any additional cash reserves should be placed in accounts that can earn you more interest.

Cash savings are protected

Cash savings are protected by the government's Financial Services Compensation Scheme (FSCS).

This provides protection for up to £85,000 for individuals and £170,000 for joint accounts per provider. If you're a single person with £170,000 in savings, you could protect the full amount by investing £85,000 in two separate accounts held by different savings providers.

Inertia is every saver's worst enemy

Unfortunately, savers often fail to make the best choices about where to hold their cash. 12.6 million (nearly a third) of UK adults hold most of their savings in a current account with their main provider. As a result, they are missing out on up to £619 each in interest a year, totalling nearly £8bn, by holding their money in a current account rather than a market-leading easy access saver[1]. So, it's important to spend time considering the right places to hold cash reserves. Here are some of the main options and potential benefits and drawbacks.

High interest current accounts

These accounts often pay more than standard savings accounts. While they can be used as an easy access account, most high interest accounts will come with certain restrictions.

Check the small print – the promise may not suit your needs. For example, you may have to save a set monthly amount into the account or there could be limits on how much of your balance will earn interest.

Earn more with fixed-rate accounts

Fixed-rate accounts typically offer higher rates of interest. However, to gain maximum benefit, you'll need to lock your money away for a set amount of time. If you have a healthy emergency fund and are comfortable with the commitment and timescale, these can be great for growing your balance. The longer you're prepared to tie your money up, the higher the interest you could gain. The rate available on fixed savings has been creeping up in recent months. As of 2023, it's possible to find two-year fixed-rate accounts paying up to 6.05% interest[2]. As the Bank of England continues to battle against rising inflation, the City expects more rate rises. So, we should see the rates on fixed savings continue to rise, too.

Consider Premium Bonds – Ernie (Electronic Random Number Indicator Equipment) could deliver big

Premium Bonds are one of the most popular UK savings options. In July 2023, more than 24 million people had a total of £121 billion of savings allocated to the National Savings & Investments (NS&I) monthly prize draw[3].

Instead of earning interest, each £1 bond is an entry into the prize draw. All prizes are tax-free and range from £25 to £1 million. Premium Bonds are also Treasury-backed and 100% secure. The downside is that, with no interest being paid, if Ernie doesn't draw your number you'll effectively be losing money as your savings won't be keeping up with inflation. You can save from as little as £25 and the maximum you can hold is £50,000 – a couple can invest up to £100,000.

Cash can create additional leg work

Because interest rates and offers are constantly changing, ensuring your cash is working as hard as possible can take a lot of time. Fortunately, there are services that we offer that can do all the work for you.

For example, our solutions removes the complication by securing optimal interest rates for your cash deposits across a variety of banks. This simple proposition helps you to reduce risk, increase potential returns on your cash, and save time.

1 www.atombank.co.uk
2 www.moneysavingexpert.com
3 www.moneysavingexpert.com

The value of investments and any income from them can fall as well as rise and you may not get back the original amount invested.

Tax concessions are not guaranteed and may change in the future. Tax free means the investor pays no tax.

Get in touch

We can help you understand how much emergency cash to keep on hand and how best to allocate additional cash reserves alongside your diversified portfolio. **Please get in touch to arrange a time to chat.**

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