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MONEY BOX

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LEWIS: Hello. Happy New Year and welcome to this special Money Box looking ahead to saving, spending, investing and buying a home in 2011 - in the context of course of how last year left us feeling. With all the talk of rising prices, looming redundancies, government cuts, lower benefits and VAT going up on Tuesday, how are people preparing for the year ahead?

FEMALE 1: I try not to think about it because it makes me depressed. Everything's just gone up - the gas, the electric, food. It's just really difficult.

FEMALE 2: You've just got to budget.

FEMALE 1: You lose luxuries really, definitely. *(laughs)*

FEMALE 2: I think it's the last year that we'll spend as we do. We'll shop in Marks and Spencer's, we'll shop in Sainsbury's, but probably next year we won't be shopping in those shops.

FEMALE 1: Yeah.

FEMALE 2: We'll be shopping somewhere else which will suit our pocket.

MALE 1: We'll just have to get on with the 14.5% rise in VAT because it's not 2.5%. It's 2.5% of 17.5%, which is considerable. I think we'll just have to carry on saving as we do and we'll just have to cut our cloth. It's as simple as that.

LEWIS: People in North London with their thoughts of how they'll react to the New Year economic climate. And two things that affect all of us are of course inflation and interest rates. The year has ended with inflation high and rising: 4.7% on the old Retail Prices Index measure, 3.3 on the one the government prefers - the CPI - but even that way above the target the Bank of England is supposed to hit of 2%. The bank of course is supposed to control inflation by adjusting interest rates, and with inflation high we would expect normally rates would go up but they've been stuck for nearly 2 years at the record low of 0.5%. The employers' organisation, the CBI, says that rates should rise, perhaps to 2.75% by the end of 2012. But Howard Wheeldon, Senior Strategist at BGC Partners, thinks that wouldn't control the rise in prices.

WHEELDON: Inflation is rising because of events totally outside of our control. Oil price demand, demand for food, commodity prices rising because of the global recovery elsewhere have all put pressure on inflation that we cannot control. We have to pay the same prices for these imported products and of course we import a lot more today than we ever used to.

LEWIS: Can the Bank of England control it by its one mechanism which is adjusting interest rates?

WHEELDON: That is the problem, it won't make any difference at all - save that it could possibly slow down the amount that we actually spend in part, but it would take a long, long time to come through. The impact that we're seeing from inflation now is very much at the top end - i.e. it is the actual commodity products that we import. It isn't necessarily at the bottom end, what you and I as the consumer buy in the shops.

LEWIS: But the CBI, the employers' organisation, has said interest rates should go up, and they're even suggesting they could be as high as 2.75% getting on for the end of 2012. Do you think that would be a sensible policy?

WHEELDON: If that was to occur, I'm afraid the UK economy would come to an absolute grinding halt. Is that what we want? I don't think we do. We're going through some very, very difficult times. We need to have a balance here. Leaving the rates as they are or just edging them up a touch is enough, I think, in 2011 to lead to the status quo. It's the status quo we want here. We're going through very, very difficult times with the cuts that the government is making and we need time. We don't need to strangle off what little growth there is.

LEWIS: Howard Wheeldon. So where will bank rate go over the next couple of years? With me is David Kuo, Director of financial website Motley Fool. David, your rates view?

KUO: Well as far as I'm concerned, if inflation is running at around 5% then the Bank of England base rate has to be above 5%. That is the only way they will be able to control the rate of inflation in the UK. The Bank of England only has one job to do. Its job is to keep a lid on inflation and that therefore means that rates have to be above the inflation rate, and we're talking here about the Bank of England base rate and that is 5%.

LEWIS: Yes. And you agree with Paul Fischer then, the Bank of England official who's also on the Monetary Policy Committee, who said just before Christmas the public should realise bank rate should return to a more normalised position, which is about 5%, isn't it?

KUO: Absolutely correct. And in fact they should have done this a long time ago. Had they done this a while ago, then we may not have had the kind of inflation that we're experiencing now.

LEWIS: Justin Urquhart Stewart's also with us. He's the Director of Seven Investment Management. Justin, do you agree? Do you think inflation has to be controlled by putting rates up?

URQUHART STEWART: Well one of the issues actually the government quite likes is a certain amount of inflation because of course it erodes debt. Those of us of a certain age will remember double digit inflation, which actually eroded significant debt at that stage. The trouble is of course if you have a bit of inflation, you end up with a bit more. What they need to be able to do is to make sure they get steady growth. But unfortunately if you put rates up by even a small amount at the moment, it'll affect those people with tracker mortgages and consumer spending, and the concern over people's debt will really hit home very quickly.

LEWIS: Yes, Melanie Bien is also here. She's a Director of mortgage brokers Private Finance. Melanie Bien, a rate rise really would hit the housing market, wouldn't it?

BIEN: It really would. I mean we've seen some worrying statistics that show that some people are already struggling to pay their mortgages and that's with interest rates at record lows. Were they to rise as significantly as some forecasters say they need to, then people could be in serious trouble, so I think that needs to be borne in mind as well.

LEWIS: On the other hand, of course, people who have savings would welcome better rates. Andrew Hagger's here too. He's from the price comparison site Moneynet. Andrew Hagger, savers would really be glad if rates went up.

HAGGER: Very much so. They've had nothing to smile about for you know 21 months now and even the fixed rate savings rates have tumbled over the last 12 months, so they would welcome a rate rise - especially those without a mortgage anyway.

LEWIS: And do you think a rate rise would feed through into the rates you actually got on your savings?

HAGGER: I don't think the full amount would feed through. I think the banks and building societies would use this as an opportunity to rebalance their profit margins a little bit.

LEWIS: Well that's the big economy. Let's look at some of the specifics. Let's look at housing - house prices and mortgage availability. And to get a sense of the market, our reporter Bob Howard went to Norfolk with first time buyer Dave Webster and property investor and consultant Henry Pryor. Dave shows Bob and Henry round the three bedroom terrace house he wants to buy in Norwich.

WEBSTER: So we've got the entrance, a small entrance porch. It's a brick addition to the building. This is the front room. The reason why I like this house is because it's tidy and as a first time buyer either it's got to be fairly move-in-able and relatively cheap or even cheaper and need some work done. Coming past the stairs into the back room, which is the kind of dining room - which once again is nice and tidy, got a nice feature fireplace and has been decked out I think for sale - bits and pieces. But a relatively high ceiling as well, probably about eight foot or so, eight and a half feet. And then into the kitchen, which does need a bit of work as far as I'm concerned. When you move into a house - and I've been looking at this - it's kitchens and bathrooms that generally need to be polished.

HOWARD: And how much is it on for?

WEBSTER: It's on for 120. It has been on the market for a fair while, so ideally I'd like it just over the 100 mark really.

HOWARD: And how realistic is that at the moment, do you think?

WEBSTER: I think personally at the minute vendors just want a little bit too much for their properties. They could have bought at a very, very buoyant time for the property market. They now want to shift it, but they don't want to lose as much money. So I think you've got to take a punt and the vendor's got to be realistic really.

HOWARD: With your deposit, did that take a long time? Did you save it up? Did you get any from your parents or any help?

WEBSTER: I haven't had any help at the moment. I had a relatively good job. Squandered most of it, went travelling on the savings; but knew I needed a little bit, so kept that behind. I've got the minimum deposit that they want at the moment, which is around about 25/30% to get a reasonable rate. And it's a long-term mortgage, so that I can pay it.

HOWARD: Henry Pryor's been doing his research as well. And having looked around, Henry, would you buy it? And, if so, what price?

PRYOR: I think the important thing for this property and the for the future value through the next 12 months is that whilst most of the commentators are taking a reasonably pessimistic view of prices falling between perhaps 5 and 10%, I think let's remember that it will be Dave's deposit that he's saved so hard over the last 2 or 3 years to put down in order to buy the house that is exposed if house prices fall.

HOWARD: You're putting the fear of God into him.

PRYOR: Well I think that people do … You know like so many things in life, it is terribly easy to rush in, to be overwhelmed by something which does look attractive, looks like it ticks all the boxes, but at the end of the day we have to remember that prices can go down as well as up. And when they go up, then the great thing about property is that you're multiplying your stake significantly by leveraging it, by borrowing the money from a lender; but when prices go down, it's that stake money that's at risk.

HOWARD: So what should Dave pay for this? What would be a decent buy in your mind?

PRYOR: It started off at an unrealistic level, optimistically £130,000. It's now at 120, so I'm talking about knocking 20% roughly off the price. And I don't think the market through the remainder of 2011 is going to fall by that sort of amount, so I think that if he can secure it at £100,000, he's probably making sure he's bought it as competitively as possible.

HOWARD: So, Dave, is that a factor in your mind that if you buy now prices could conceivably drop further?

WEBSTER: If house prices drop, you may lose some money. If house prices increase, you've still got to buy somewhere that's more expensive than what it would be at today's rate. I like it and I think if the vendor was to move on price a little bit, I would be happy to put in an offer. If they don't want to sell it at that price, I've got no issues with walking away.

LEWIS: Dave Webster showing how to negotiate. And the word 'move-in-able' is one I don't think we've had on Money Box before. It's a very nice one, Melanie Bien, isn't it? But can buyers really beat sellers down by 20%?

BIEN: That's quite a drop, isn't it? I think a lot depends on the house in question - you know whether it's highly desirable, in a fantastic location, whether it's been on the market for months on end, how realistically it's priced in the first instance. You really need to do your research - I think what that piece shared there - really see what similar properties in the area are going for and get a feel for what the seller wants from it as well, talk to the agent.

LEWIS: Yes and what about mortgage availability? I mean Dave Webster's done what we all advise: he's got a big deposit - probably something like, what, £30,000 from what he says. That's more than most people earn in a year. It's quite hard to save up that sort of money.

BIEN: Yes, first-time buyers are finding it particularly difficult. Lenders require at least a 10% deposit, and again you need about 25 to 40% if you want to access the best rates on the market. If you don't have that, you only have 10%, you're looking at paying about two percentage points more than for someone with a 25% deposit. So it is significant.

LEWIS: And what kind of best rate can people get now? If they've got that big deposit, what are we talking about on a good mortgage?

BIEN: Well you can get 5 year fixes for about 3.89%, 2 year trackers for less than 2%. So there's some amazing deals out there at the moment.

LEWIS: And do you think people should be fixing because if interest rates are going to go up, and almost everybody thinks they are over the next few years, that will push up the cost of mortgages; but if you fix now at you know 3 or 4%, then you're doing very well?

BIEN: Well historically those are fantastic rates and, yes, it buys you security over a longer period of time. And we would suggest 5 years rather than 2 because if interest rates do start going up next year and the year after, with the 2 year deal you'll have to remortgage again just as rates are higher. So 5 years buys you security for longer.

LEWIS: And Justin Urquhart Stewart, how do you see the banks and mortgage availability? Are they really doing what they should be doing or are they starving us of funds?

URQUHART STEWART: It's still going to be very constricted indeed. We haven't seen the full reforms of the banks going through. We saw Northern Rock being very well reorganised and it's now back in the market again, but the likes of RBS and Lloyds still need significant restructuring to make them fit for purpose. So I'm afraid the banks are going to go through difficult times in 2011, particularly with not so much their capital but they need to refund a lot of their financing and that's going to make life more difficult for their lending.

LEWIS: You mean they've got to borrow it again themselves …

URQUHART STEWART: Absolutely.

LEWIS: … and that makes it difficult for them to get the right sort of rate. Melanie Bien, last year you told us, about this time of year you predicted prices would fall about 6%. They haven't, have they? They've risen very slightly. What went wrong with your thoughts? *(Bien laughs)* I'm not putting you on the spot in that sense, but why did you think they'd fall but they haven't? What's changed?

BIEN: Well the market outperformed expectations in the first half of this year incredibly. You know house prices just kept rising. And in the second half of the year, we have seen falls again and we expect falls to push into next year. What would have been seen this year actually has been pushed back a bit. So I'm not as pessimistic as others. I think we'll end this year at about you know flat or with a slight drop.

LEWIS: Because we still have those old issues of supply and demand, don't we? There seems to be a big demand for property; there are mortgages if you've got a bit of money. And yet we're not building as many and under the government's plans, we'll be building even fewer.

BIEN: Yes, there is a finite number of properties available and we've seen there'll be much more demand for rental property next year as first time buyers can't get on the ladder. And that in turn will bring buy-to-let landlords back out of the woodwork if they can get the finance.

LEWIS: Well saving for a deposit of course is step one of buying a home for most people, but saving needs a certain state of mind and Ruth Alexander found some determined savers in North London.

MALE 1: If you want something bad enough, you will save for it and you will do without various things until you have enough money to buy what you want.

FEMALE 1: Ever since the recession hit a couple of years ago, I think everybody has had to really rethink the way they spend. I kind of look at the way I was in my twenties and I kind of think what do I have to show for it really? So saving to me is much more about intellectually now because I know there is so much more I will gain from it in the long-term.

FEMALE 2: I was a saver. Now I'm a spender. Not worth saving now. *(laughs)* Before when it was a good interest, that was worth saving. But now, I'm only making the bankers richer and me poorer.

FEMALE 3: I would use any money first of all to pay off my mortgage because the interest rates are always going to be lower than the mortgage rate, so ultimately that's the way to save.

MALE 2: I'll put you know a proportion of my income away every month. I think psychologically you've got to get into that position where you know that it's not really your own income, therefore don't touch it.

ALEXANDER: And what's going to happen at the end, once you've accumulated a certain amount? Will it become yours and you'll spend it on something? Or do you think you'll never spend it?

MALE 2: I honestly think I'll never spend it.

LEWIS: Well if saving is a state of mind, perhaps you don't look so closely at the rate of interest being earned and perhaps that's just as well. And despite very low rates being paid, there is more cash going into saving. The amount rose £4.6 billion in November. Andrew Hagger from Moneynet, what's the average return you get now on an instant access savings account?

HAGGER: Pretty poor. It's just below 0.7%, so you can see why perhaps some people are sort of giving up their savings habit a little bit.

LEWIS: Yes, but of course you can get a lot more than that if you're a bit busier in the year and you move your money around every 6 months or every 12 months, can't you?

HAGGER: Yeah, I mean there are a range of instant access accounts where you can get almost 3% now. You can get 2.9 with the Post Office. But all these deals have a significant bonus built in for the first 12 months, so it's a case of having to keep switching, I'm afraid.

LEWIS: So you do keep moving every year. And what about locking your cash away? I mean particularly if you're saving up for a deposit for a house, for example, you might think well this is going to take me 5 years, so the first lot of money I put in, I can lock away for 5 years.

HAGGER: Well I mean if you're able to do that, then you know that's where you get the better rates. It's currently 4.75 for 5 years, but you do need to be absolutely sure that you're not going to need to touch that money in the meantime because in most instances you won't be able to get it out if you do.

LEWIS: You'll get a big penalty if you do. And David Kuo, I know you believe in investment for making money, but everyone should have a bit of money in cash, shouldn't they?

KUO: Oh absolutely right, you should have a cash cushion to sit on. And I'm talking at the moment about 6 months worth of household expenditure that you should have readily available because if you do lose your job, it could take you 6 months to find the next one, and that is why you need a cash cushion.

LEWIS: Yes and that's a lot more than most people have, I'm sure. Melanie, let me just ask you, are you a saver or a spender? Which side are you on listening to those people in North London?

BIEN: Well I'm a little bit old-fashioned. I think you shouldn't really spend money you don't have.

LEWIS: So you don't whip out the credit card?

BIEN: Well I do, but I pay it off every month, so boring like that.

LEWIS: Boring, but very, very sensible, yes. And saving up. I mean Andrew Hagger, is there any evidence people are really saving up and then buying stuff, or are they just saving up for its own sake?

HAGGER: I think they're saving up just in case because at the moment there's a lot of fear out there on the back of the government spending cuts that were announced. A lot of people are perhaps concerned that their job may not be safe and so I think they're just putting money aside just for a bit of a safety net really.

LEWIS: So really, as David Kuo was saying, having a few months in the bank anyway, so if you do lose your job at least you can pay the bills until hopefully you'll get another one?

HAGGER: Exactly, yeah.

LEWIS: And can I just ask you one final thing, Andrew. We've talked about low savings rates and, a rather gloomy thought, they may not go up even if rates go up. Is the problem really a lack of competition; there's no new players in there who are offering good deals, permanent good deals for people?

HAGGER: I think that's partly the problem; we haven't seen any new players on the market for a while. I mean I know Metro Bank have opened, but I think they're still relatively small in the scheme of things.

LEWIS: And offering low rates certainly. It's 0.5% I think on their instant access account. Though they do interestingly have savings you can tie up for as little as 3 months and get a slightly better rate.

HAGGER: Yeah, I mean if you're looking at 3 months, you're just as well really I guess to look at some of the instant access accounts that are out there at the moment because, as I say, you can almost get 3% on those.

LEWIS: So certainly the banks are being told they've got to be more competitive and we'll have to see what happens on that. But of course with savings rates so low, as we've been discussing, many people are tempted to invest their money in the hope they will make more. And of course there is that chance of making more. With the benefit of hindsight, we can see that share prices have risen by around 10% this year. The price of gold is up more than 25%. But is investing rather than saving sensible? Could gold and even shares be at their peak? Justin Urquhart Stewart, gold up hugely. Now copper I read is at record highs, other metals very high. Is that the time to buy or to sell?

URQUHART STEWART: Well, as ever, as soon as things reach an all time high, that's not the time to be rushing in. Now is the time actually to be suitably circumspect, to understand why it's gone so high, and the answer is the demand in terms of what you've seen in China in terms of copper and in terms of gold because of the fear that is in terms of what's happening in the global economy. So if you believe that actually global fears are overdone and that the Chinese economy will still grow but maybe a bit slower, then maybe that growth isn't going to be there in the same way as it was before. So don't follow this year's fashion fad. It is next year's tank top.

LEWIS: I can just imagine you in a tank top, Justin.

URQUHART STEWART: *(laughs)* Thank you.

LEWIS: With your braces. If you did want though to invest in say copper. I mean gold is easy in a way - people go out, they buy a bit of gold - but if you wanted to invest in copper or other metals, what kind of instrument is there for doing that?

URQUHART STEWART: Well you've got to be careful. There are some very good exchange traded funds, which are merely funds which enable you to track the price of copper. You need some advice as to which ones to choose to make sure you're dealing with actual real copper, and also in terms of the pricing of it because it can be affected by some of the derivatives or futures tradings markets. So those are quite simple. Alternatively, of course, you can actually buy via some of the mining companies themselves, which are not obviously directly related to the copper price, but obviously impacted by it.

LEWIS: Yes and of course hope to get some windfall if they suddenly discover something but then lose money if they don't, as happened quite recently. And David Kuo, if you are trying to grow your money perhaps but you're a bit cautious because you've just come out of cash and you don't really want to lose much of it, where's the best place to start?

KUO: Well one place to put your money is in these high yielding shares. I mean these are companies that pay a generous dividend. They make a lot of profits and they share some of their profits with their investors. And so what you can do is to build yourself a nice group of high yielding shares and then just sort of drain off the dividends throughout the year.

LEWIS: You have the dividend, so of course the value of the capital you've got may go down or up by the end of the year. But just give us some examples of companies that do pay high dividends.

KUO: Well if you're having a look at utility companies, I mean these are companies that can ratchet up their prices whenever they want. They can do anything with prices that they want to and as a result of that they can generate a very nice lump of profit at the end of each year, which they share with shareholders.

LEWIS: And how about retailers?

KUO: I would be very disinclined to invest in retailers in 2011 because I have a feeling that consumers are going to be very, very sort of tightly crimped as far as discretionary spending is concerned, which means that they won't be able to spend as much on the high street.

LEWIS: And Justin Urquhart Stewart, what about the emerging economies - China, India, Brazil, Russia and so on? Do you think they're a good bet if you want to put some of your money outside the UK?

URQUHART STEWART: The longer term future for these areas and other developing nations is very positive indeed. However be careful - an awful lot of money has been chasing what are often very small markets. And the much over-hyped BRIC - Brazil, Russia, India and China - well funnily enough in the past year, they were well overtaken by the rather dull FTSE 250 index, which is the rather domestic UK index, which everyone thoroughly ignored. So for the future - yes, if you're willing to take a longer term view; but in the short-term, be wary, these are emerging markets.

LEWIS: And David Kuo, the FTSE 250, that's the 250 biggest companies below the top 100. The top 100 is very much an investment in foreign parts, isn't it, whereas the 250 is much more an investment in UK firms?

KUO: Oh quite right. I mean let me give you an example of some of the companies in the FTSE 100. Some of these companies are almost unpronounceable. You've got Kazakhmys, Vedanta, Xstrata. I mean that looks like a bad collection of Scrabble letters that you have. Then you've got Antofagasta, Fresnillo. So if you want some exposure to overseas markets, the FTSE 100 is as good a place as any.

LEWIS: And hope to get a triple word score. And let me just ask Melanie Bien briefly on this investment side. Is property a good investment or should we just see it as a roof over our heads?

BIEN: I think we should see it as a long-term roof over our heads. People are staying in their properties longer. They're seeing that it's not the place to make a quick buck by buying and selling, and I think it's positive that people are finally getting their heads round that. If prices fall in the short-term, over time they tend to rise, so not to get too panicked about it.

LEWIS: Yes because your house is still worth one house whatever happens to property prices - up or down - isn't it?

BIEN: Exactly.

LEWIS: Well we've had a few predictions during the last half hour, but it's on the spot time now for our experts. And I'm going to let each of you choose your own prediction - share prices, interest rates, inflation, house prices. Whatever you want, you choose. So it's your best shot at your best topic. Where will it be this time next year? And no lengthy explanations. A quick forecast and a quick reason. Let's start with David Kuo.

KUO: For me, the FTSE 100 should hit 7000 next year, and at a push it could go as high as 8000 points.

LEWIS: So that's above its previous record of, what was it, 6900 and something, wasn't it?

KUO: Absolutely correct.

LEWIS: Melanie Bien.

BIEN: House prices flat or a slight drop of about 1%.

LEWIS: Right, so that's not such bad news as you were warning us about last year.

BIEN: No.

LEWIS: Let's hope that's right. Justin Urquhart Stewart?

URQUHART STEWART: A broad range of asset classes, including shares, should give you a 7% return. So part of that with the FTSE 100, which I would say should be about 6,666, which sounds a bit sinister.

LEWIS: So that's your prediction. And asset classes, you mean spread your bets - have something in commodities, something in property, something in the FTSE 100?

URQUHART STEWART: Absolutely. Don't just rely upon one or two.

LEWIS: Andrew Hagger, what's your prediction?

HAGGER: I'm going to stick my neck out and say that I think base rate will double next year and will end up at 1% with stubborn inflation being the reason.

LEWIS: Right. There are four predictions from people. We'll see how you do a year from now. But that's it for today. Thanks to all my guests. That was Andrew Hagger from Moneynet; Justin Urquhart Stewart of Seven Investment Management; Melanie Bien of Private Finance; and David Kuo from Motley Fool. You can find out more on our website, bbc.co.uk/moneybox, where you can sign up to my weekly newsletter or just read it now; download a podcast; listen again; send us your ideas, and why not let us know your 2011 predictions and concerns. I'm back on Wednesday with Money Box Live - this week taking questions on consumer rights when things you've bought go wrong or didn't even arrive. Back with Money Box next weekend. Meanwhile there's money news 24/7 on my Twitter - Paul Lewis Money. Today from reporters Bob Howard and Ruth Alexander, producer Lesley McAlpine, and from me, Paul Lewis, have a good 2011.