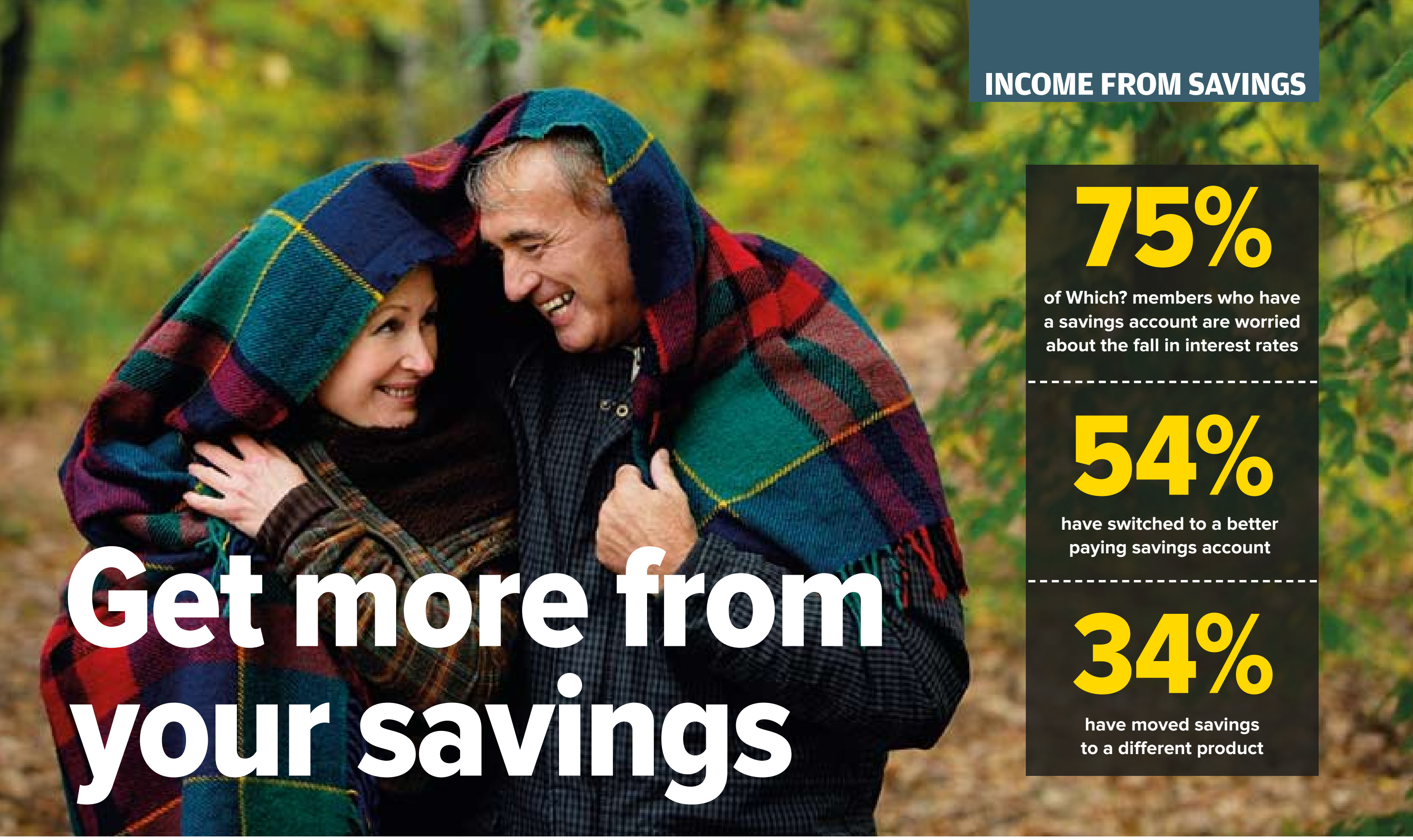


Get more from your savings

75%
of Which? members who have a savings account are worried about the fall in interest rates

54%
have switched to a better paying savings account

34%
have moved savings to a different product

Need income from your savings? We look at ways of making your money work harder when interest rates are low

Over the past two years, interest rates have fallen drastically – bad news if you rely on your savings to supplement your income. The best cash Isa, for example, paid 6.21% in August 2007, compared with 3% this year. On £10,000, that's a difference of £321 a year.

If you have a taxed savings account rather than an Isa, you need to earn at least 2.25% gross interest if you're a basic rate taxpayer, or 3% if you pay higher-rate tax, just to keep up with inflation.

When we surveyed 3,695 Which? online panel members about their savings in August 2009, 75% of those with savings said they were worried about the fall in rates.

Better than the bank?

If the income on your savings is not stretching far enough, other investments may generate a better return. But you'll have to take some risk with your capital so, although you may get a much better return, you could end up with less than you started with.

Before you invest, remember the importance of diversification – don't put all your eggs in one basket, because nothing performs well all of the time. And don't invest unless you can do so for at least five, but preferably 10, years.

You should seek independent financial advice to make sure your investments suit your circumstances. Look for a financial adviser with qualifications that are higher than the minimum level (see www.which.co.uk/ifaqualifications).

So where might you find a better return than the bank or building society? The table, right, shows the typical income you'd get, net of basic-rate tax, on an investment of £10,000. The risk rating runs from high to low. The types of investment are explained below.

Gilts

When you buy gilts, you're lending money to the UK government in return for a fixed income. They're one of the safest investments you can make – the UK government has never failed to make interest or capital repayments, although that's not to say it couldn't happen. Available gilts are listed at www.dmo.gov.uk.

You can buy gilts yourself or through an investment fund (see p71). The main advantage is that they pay a fixed amount of interest over a fixed term, so you know what you'll get and for how long. You'll pay tax on any income unless you buy gilts through a stocks and shares Isa. Capital gains are tax-free.

The best cash Isa paid 6.21% two years ago, 3% in August this year

TYPE OF INVESTMENT	NET ANNUAL INCOME ON £10,000	RISK
Equity income fund	£400-£650	HIGHER
Corporate bond fund – high yield	£560-£800	
Corporate bond fund – investment grade	£400-£560	
Ten-year gilt	£382	
Five-year gilt	£285	
Two-year gilt	£161	
One-year fixed-rate cash Isa	£320	
Cash Isa	£300	LOWER

Notes: There is a risk of capital loss with gilts, corporate bond funds and equity income funds. Gilt figures shown are based on the gross redemption yield, which is a measure of the total before-tax return you will get if you hold the gilt to redemption. Cash Isas are tax-free. Returns are not guaranteed other than with cash Isas and gilts held to redemption. Table correct at 25 August 2009

However, unless you opt for index-linked gilts, your income and capital won't be protected against inflation. And you won't necessarily make a capital gain. Most gilts are priced 'above par' at the moment, which means that if you bought them today, you'd make a loss if you held them to redemption (the end of the fixed term). Gilts are listed on the stock exchange, so you can sell them at any time, but the price fluctuates. If interest rates and inflation are rising, prices usually fall and vice versa.

Short-term gilt yields are currently very low. In September 2009, two-year gilt yields were around 1.5%. Ten-year gilt yields were around 3.75%. Neither compare very well with savings accounts.

Corporate bonds

Corporate bonds are similar to gilts, but instead of lending to the government you lend to a company. This makes them riskier because there's a greater chance of a company defaulting on its loan. But because of this extra risk you can expect higher yields than with gilts.

The risk of companies defaulting means that buying individual corporate bonds isn't a good idea unless you can buy a lot to spread the risk. Instead, the

usual way to invest in corporate bonds is through an investment fund (see opposite). Your capital can rise and fall in value as the fund trades the bonds on the stock market.

In August 2009, investment-grade bond funds (those investing in companies with the highest credit ratings) were quoting yields of around 5-7%, but this can vary and isn't guaranteed. High-yield bond funds (those investing in companies with low credit ratings) quote yields of around 7-9% .

These yields take into account the annual fund charge and any additional charges, but no initial charge. They're gross of tax – you'll pay income tax at your usual rate on any income unless you invest through a stocks and shares Isa. Be careful, because high yields can be misleading. Some funds pay charges out of capital, rather than income, which increases the yield but limits capital growth potential. Unless you're willing to take a significant risk with your money, stick to the less risky investment-grade bond funds, and always seek independent financial advice.

Equity income funds

Equity income funds are a type of investment fund. They aim to produce income by investing in the shares of a range of companies that pay good dividends. As an investor, you would also hope for some capital growth over time, giving you protection against inflation.

These funds are riskier than gilts and corporate bonds, and you must be prepared to see your investment and income fluctuate in value. For most funds you'll need to have a lump sum of at least £1,000 to invest.

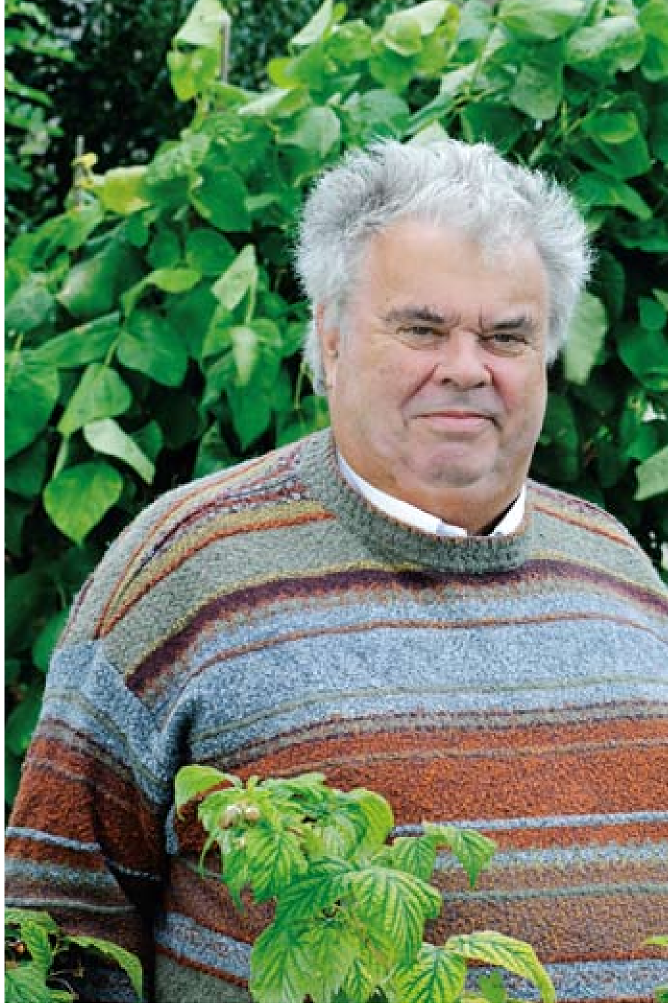
Equity income funds were quoting yields of around 4% to 6.5% at the time of writing. But bear in mind that these are historic yields based on the dividends the fund paid out in the previous year. They aren't guaranteed, and you could get less.

Also, although share prices have been low recently, companies have been paying out reasonable dividends – making equity fund yields look high. This situation is unlikely to last, and you shouldn't expect much more than 3-4% from an equity income fund in general.

Tax of 10% is deducted before the income reaches the fund. If you're a basic-rate taxpayer you won't pay any more. Higher-rate taxpayers have a further 22.5% of the gross dividend to pay, but you can avoid this if you invest through a stocks and shares Isa. The 10% tax cannot be reclaimed.

Purchased life annuities

You probably associate annuities with your pension, but you can buy a temporary annuity (one that pays out for a set number of years) or a lifetime annuity with any savings you may have. You hand over a lump sum (you need at least £5,000) and receive a guaranteed income in return. In August 2009, a 65-year-old man could expect to receive an income of between £564 and £632 a year for every £10,000 invested. A woman would get slightly less because of longer life expectancy. The older you are when you buy the annuity, the more income you'll get. You will also receive more if you have certain illnesses.



WHICH.CO.UK

Find out more about stocks and shares Isas at

www.which.co.uk/stocksisas

Remember that your income will lose buying power over time. You can try to combat this by buying an index-linked annuity. However, these generate lower rates of income (a 65-year-old man could expect just over £300 a year for a £10,000) investment), so you'll need to decide whether it's worth it.

One of the advantages of purchased life annuities is that some of your income is treated as a return of your capital for tax purposes. That means you'll only be taxed on part of your income rather than the full amount.

Other products

Structured products and investment bonds are often heavily sold to those looking for income. But Which? has serious reservations about both. To find out more, see **www.which.co.uk/structured products**. See **www.which.co. uk/money** for more on savings and investments.

PHOTOGRAPHY GETTY IMAGES, ALAMY, JASON INGRAM

INVESTMENT RETHINK

Terry Yearsley, 63, semi-retired

Five years ago, Terry Yearsley moved his savings from a Tessa into a fixed-term investment with HSBC. It matured this year and, although it returned his capital, he earned only £350 – a dire return on his original investment. His shares in RBS, which previously gave a good return, have also taken an enormous hit.

Terry says: 'I want to recoup my losses and earn income. I've chosen lower-risk investments – corporate bond funds – and put them into a stocks and shares Isa because of the tax advantages.'

WHAT IS AN INVESTMENT FUND?

If you don't want to go it alone, you could turn to a fund that will invest your money on your behalf

Investment funds lower your investment risk because your money is spread across a wider range of companies than it would be if you invested by yourself. There are several types, including unit trusts, open ended investment companies (Oeics) and investment trusts.

Your money is pooled with cash from other investors and is invested on your behalf by a fund manager. You can invest as little as £500 as a lump sum or £20 a month, and your money will be spread across a range of companies or assets.

Investment funds cover all sorts of different investments and levels of risk – from UK gilts to shares in emerging markets.

You pay an initial charge, an annual charge and additional fund charges to cover items such as legal and trustee fees. However, the initial charge is discounted if you buy through a discount broker or fund supermarket.

Picking the right investment fund can make a big difference to the return you make on your money. For example, the best equity income funds have generated total returns of more than 50% over the past five years, while the worst have lost investors money.