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Winter Newsletter 2017

Despite numerous geopolitical threats (Eurozone elections, tensions between the US and China, North Korea etc.), worries about the demise of the so-called "Trump trade" and shares being overbought and due for a correction at the start of the year, sharemarkets have proved to be remarkably resilient with only a minor pull back into their recent lows. We have also seen the Federal Budget released in May which is about the "right choices" and being "fair and responsible". When translated into Treasurer-speak, means "I never want to hear anyone mention the 2014 budget ever again...". Following is a summary of the key issues arising from the Budget and how they may affect you.

Federal Budget 2017-18

The 2017-18 Federal Budget was handed down on Tuesday 9 May. If you are working, retiring, or have already retired, you could be impacted by a number of changes.

It is important to discuss your particular circumstances and how these changes apply to you, with your financial adviser.

Note: These measures are proposals only and may change or not eventuate at all until passage of legislation through parliament.

Superannuation

Contributing the proceeds of downsizing to super

From 1 July 2018, people over age 65 who sell their family home may have the opportunity to make a one-off contribution of up to $300,000 of the proceeds from the sale to their super. To qualify, the home which is being sold must have been their main residence for at least the previous ten years. If the home is owned jointly by a couple, each person will be able to access the $300,000 threshold.

It is important to note there are no provisions for social security means testing exemptions on these contributions - once made, the funds will be assessed as standard superannuation monies.

First Home Super Saver Scheme

From 1 July 2017, super can be used to assist with saving for a first home purchase. Up to $15,000 per year of voluntary contributions (which appears to capture both concessional and non-concessional) can be contributed to super, and then be available to withdraw for the purposes of purchasing a first home. A total amount of voluntary contributions of $30,000 can be made available under the scheme. These contributions must be made within existing concessional and non-concessional contributions caps.

These contributions will also accrue 'deemed earnings' calculated at the 90-day bank bill rate plus three percentage points (4.79 per cent per year deemed earnings based on the March 2017 rate). These earnings will be withdrawn along with the contributions when a home purchase is made.

On withdrawal, concessional contributions and deemed earnings will be taxed at the individual's marginal tax rate, less a 30 per cent tax rebate. It is presumed non-concessional contributions are to be withdrawn tax-free. First Home Super Saver accounts are created on an individual basis – meaning each member of a couple can have their own account. Importantly, the release of funds to purchase a home will not count as income for certain tests, such as HELP/HECS repayments, family tax benefits or child care benefits.

Changes to Limited Recourse Borrowing Arrangements (LRBA)

From 1 July 2017, the borrowings under a LRBA are to be counted towards an individual's pension transfer balance cap.

Taxation

Medicare Levy Rate

From 1 July 2019, the Government will increase the Medicare levy by half a percentage point from 2 to 2.5 per cent of taxable income to ensure the National Disability Insurance Scheme (NDIS) is fully funded and to future guarantee the Medicare system.

Medicare Levy low income thresholds

From the 2016/17 income year, the Government will increase the Medicare levy low-income thresholds for singles, families, seniors and pensioners to take account of movements in CPI so that low-income taxpayers will generally continue to be exempt from paying the Medicare levy.

The threshold for singles will be increased to $21,655. The family threshold will be increased to $36,541 plus $3,356 for each dependent child or student. For single seniors and pensioners, the threshold will be increased to $34,244. The family threshold for seniors and pensioners will be increased to $47,670 plus $3,356 for each dependent child or student.

Temporary Budget Repair Levy ceases

While not announced in the Budget, the 2% Temporary Budget Repair Levy for high income earners where their taxable income exceeds $180,000, has not been extended and as such will cease to apply from 1 July 2017.

Disallow the deduction for residential rental property travel expenses

Effective from 1 July 2017, deductions for travel expenses related to inspecting, maintaining or collecting rent for a residential rental property will be disallowed. Additionally, the rules around claiming depreciation will change so that deductions for plant and equipment will only be allowed where an expense has actually been incurred.

Social Security

Energy Assistance Payment

The Government will make a one-off Energy Assistance Payment in 2016/17 of $75 for singles and $125 per couple for those eligible for qualifying payments on 20 June 2017 and who are residents in Australia.

Qualifying payments include the Age Pension, Disability Support Pension, Parenting Payment Single, the Veterans' Service Pension and the Veterans' Income Support Supplement, Veterans' Disability Payments and War Widow(er)s Pension.

Pensioner Concession Card reinstatement.

From 9 October 2017 the Government will reinstate the Pensioner Concession Card (PCC) for former pensioners who lost their Age Pension as a result of the 1 January 2017 Age Pension changes. Those affected will receive the PCC and retain the Commonwealth Seniors Health Card, to ensure they continue to receive the Energy Supplement. Where they received the Low Income Health Care Card, that card will be deactivated.

This will help eligible pensioners access state-based concessions on items such as council rate, vehicle registration and utilities discounts.

Increasing the Liquid Assets Waiting Period

The Government plans to increase the maximum Liquid Assets Waiting Period (LAWP) from 13 weeks to 26 weeks, effective from 20 September 2018. The LAWP is the number of a weeks a person is precluded from receiving Government income support.

The LAWP applies to the following payments:

- Newstart Allowance
- Youth Allowance
- Austudy payment
- Sickness Allowance.

Federal Budget 2016-17

These measures were previously announced in the 2016-17 Federal Budget on 3 May 2016 and are now legislated to take effect from 1 July 2017.

Transition to retirement income streams

From 1 July 2017, the tax exempt status of income from assets supporting transition to retirement (TTR) pensions will be removed.

Transition to retirement pensions allow individuals to access their superannuation whilst still working between preservation age (currently 56) and age 65. Under the new rules, people can continue existing TTR pensions and start new ones; however, the earnings on these assets will be taxed at 15% in line with accumulation assets.

Transfers to pension accounts capped at $1.6 million

From 1 July 2017, a $1.6 million cap on the total amount of superannuation that can be used to commence a pension will be introduced. New rules will limit the amount that individuals can transfer into on allocated pension. The $1.6 million cap will increase in $100,000 increments in line with the Consumer Price Index (CPI).

If you already have Allocated Pensions but are also in receipt of a defined benefit pension, i.e. ESS Super, PSS etc, then the annual defined benefit pension amount multiplied by a factor of 16 forms part of this cap.

For those entering retirement after 1 July 2017, any superannuation in excess of the cap can remain in accumulation, where earnings are taxed at 15%. Punitive taxes will be applied to pension commencements in excess of the cap including the earnings on the excess.

For those with existing pensions on 1 July 2017, amounts in excess of the cap on this date will need to be rolled back into an accumulation account or withdrawn, before 30 June 2017.

Annual non-concessional contributions reducing to $100,000

From 1 July 2017, the annual non-concessional contributions (NCC) cap will be lowered to $100,000 (from the current $180,000) and will introduce a new constraint so that individuals with a total Super balance of $1.6 million or more will no longer be eligible to make non-concessional contributions.

Individuals under age 65 will still be eligible to bring forward three years' worth of non-concessional contributions. Under the new rules, from 1 July 2017, the new year bring-forward cap will be $300,000 (down from the current $540,000 cap).

Annual concessional contributions reducing to $25,000

The concessional contributions annual cap will reduce to $25,000 for everyone from 1 July 2017. Currently they are $30,000 for those under 50 and $35,000 for those over 49. Some clients will need to reduce their super salary sacrifice amounts.

Sources: IOOF & Challenger

End of Financial Year Reminders

Super Contributions

Concessional

Review your employer or personal tax deductible super contributions (concessional contributions) to ensure you comply with the limit cap for 2016-17 of $30,000. If you were 49 years of age or over as at 30 June 2016, then the concessional contribution limit cap is $35,000. If making a personal contribution (non-concessional), the limit is $180,000 pa. if under age 65, and the work test does not apply.

Non-concessional

Prior to 30 June 2017, the limit cap of after-tax contributions is $180,000 p.a. You can, however, bring forward 3 years' worth of contributions totalling $540,000.

CARE: Contributions from previous years may count towards these limits, so you must check with your adviser to ensure you do not breach these limits. Hefty tax consequences apply for breaches.

Co-contribution

If you are still working, under 71 years of age at the end of the financial year and your taxable income is < $36,021, then a super contribution of $1,000 after tax before 30 June gets you the full $500 Government co-contribution. If your taxable income is up to $51,021 then a pro-rata Government co-contribution will be paid.

Spouse contributions

If your spouse earns < $13,800 pa. and you make a super contribution of $3,000, you may be eligible for a rebate of up to $540.

Age pension

Age pension assets test cut offs for couples is now $821,500 and $546,250 for singles. Your home is not counted. The full age pension (excluding the pension supplement) is $609.30 per fortnight each for couples and $808.30 per fortnight for singles.

Allocated pensions

You will receive a notification in July of your new minimum allocated pension payment amount. If this needs to be changed simply send the forms back to increase your pension or change the frequency of your payments.

Update your email address

For those of you who would like to receive some of the information we send in a timely and environmentally friendly manner via email, please contact us at reception@investorwealth.com.au.

Earnings, Unit Pricing and Returns

Every year in July we see delays in unit prices due to the end of the financial year. This invariably leads to delays in the switches and withdrawals being processed.

REMINDER: If you require a lump sum withdrawal in July, it may be best to have this actioned prior to the 30th of June 2017, however you need to be aware of tax implications for this year.

Question: Why haven't unit prices been updated since 30 June?

Answer: After June 30, fund managers need to conduct their end of year calculations. While this is taking place, the absolute value of the fund cannot be determined. This means they can't accurately update unit prices.

Once fund managers have completed these calculations they will issue unit prices for the day they resume pricing and all of the days for which no prices were issued.

PLEASE NOTE: This delay in unit prices will halt all switches, and withdrawals made after 1 July until the applicable unit prices are available on each individual account

Question: Why has my investment value fallen after 30 June?

Answer: Some of the managed funds you have selected may pay an income distribution for the period ending on 30 June.

Where a managed fund pays an income distribution, this will usually result in a decrease in the unit price of that managed fund and reduce the value of your investment in that option.

This will be balanced out once your fund receives the applicable distribution as a monetary amount.

Members and investors should be aware that there can be a delay from when the unit price drops, and the day the fund receives the relevant distribution.

Global growth looking healthier - underpinning sharemarket

Key points:

- Global growth is looking healthier as easy monetary policy gets traction, fiscal austerity has come to an end and memories of the GFC fade.
- This should underpin profits and sharemarket but see a resumption of a gradual rising trend in bond yields.
- Stronger global growth is positive for Australia and supports the case for the RBA to remain on hold. But with underlying inflationary pressures remaining very low and underemployment very high a rate hike is unlikely until second-half next year.

Global economy best in years

Numerous indicators point to a stronger global economy.

Business condition indicators - commonly called purchasing managers' indexes or PMIs - have moved up to their highest since the post GFC bounce.

This is the case for manufacturing and services sectors and for advanced and emerging countries. This generally points to stronger growth ahead. Believe it or not the Eurozone currently looks to be the star performer on this front.

Consistent with improving global economic conditions, measures of unemployment are heading down in the major advanced countries (albeit they still have further to go in Europe).

Asian economics, which are always a good barometer of the health of the global economy, are seeing a solid rebound in export growth. So much for all the talk that world trade and globalisation had peaked!

Reflecting the improvement in global growth, for the first time in years the IMF's latest World Economic Outlook update revised up its global growth forecast for the current year to 3.5% from 3.4% rather than revised it down as had become the norm.

Of course, there is one qualification to all these positive signs (there is always something!) and that is that the US economy looks to have seen a soft start to the year as measured by GDP growth. However, March quarters in the US seem to regularly come in on the soft side initially only to get revised up later and be followed by a bounce back in growth suggesting a seasonal adjustment problem. US unemployment claims running around their lowest since the early 1970s - no mean feat given that the US economy remains strong despite a soft March quarter.

So why the turn for the better in global growth?

There are a bunch of factors driving healthier global growth including:

- Years of ultra-easy monetary policy - zero and even negative rates and money printing - have finally got traction.
- Fiscal austerity has largely come to an end.
- Memories of the global financial crisis (GFC) and hence fears of another re-run are gradually receding - after all it is now 9-10 years ago (shares peaked in 2007!) - and so the negative impact on confidence is gradually receding too.
- Deleveraging (the desire to reduce debt ratios) post the GFC, to the extent that is occurred, has arguably run its course.

Investment implications

The pick-up in global growth is not so strong as to tell us that we are near the peak of the cycle. Spare capacity remains in labour markets, factories are still not running at full capacity, wages growth remains relatively weak (albeit it's trending up a bit in the US) and core inflation remains low. Out of interest the US leading Economic Indicator has only just surpassed its pre GFC high and historically it's taken six years on average for the next recession to start.

In other words we are a long way from boom times that then give way to a bust. Nevertheless, the implications of the healthier global economy are likely to be:

- Ongoing support for sharemarkets - as stronger growth underpins further gains in profits - which should mean reasonable returns from shares.
- Support for commodity prices - although it's doubtful they will take off given the lagged impact of rising supply but it should mean we have seen the lows.
- A bottoming in the global interest rate cycle. The Fed will continue its gradual tightening in monetary policy in the US with two more rate hikes likely this year and a start to reversing quantitative easing later this year via a phased reduction in the Fed rolling over its bond holdings as they mature. Other countries will eventually follow.

For Australia, the stronger global growth back drop is a positive in supporting export demand and confidence which in turn should help support growth pickup towards 3%. Which in turn adds to confidence that the official cash rate has bottomed. However, with downside risks to growth remaining very high, wages growth still ultra-weak, the $A remaining relatively strong and core inflation remaining below target we remain of the view that an RBA rate hike is unlikely until the second half of 2018.

Source: Dr Shane Oliver, AMP Capital

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