Personal Wealth

Winter 2014

A Quarterly Newsletter for Lifespan Clients

What's inside...

Investment Markets

Recent History

A fairly quiet few months in markets except for the situation in Europe where Russia annexed Crimea after a referendum where it is alleged that over 97% of the turnout voted in favour of joining Russia.

The major feature of markets has been a rally in higher yielding sectors with Australian listed property and utilities leading the way, up about 8% in price in the year to date (May 17). Over the same period the Australian 10 year government bond yield has fallen from 4.2% to under 3.8%.

Global bonds have also rallied. The other standout was the Australian dollar rising 5% since January which has impacted the return of overseas assets such as global equities.

In the 3 months to 30 April Australian sharers returned 2.1% while global shares returned a negative 2.4%. This difference pretty much reflected the move in the Australian dollar.

Australian Small Cap equities continued their underperformance and are about 4% behind the returns of large cap shares in the year to date.

The US Federal Reserve continued the process of winding back the quantitative easing (QE) program or "tapering". It is currently sitting at $45 billion per month which is down from $85 billion.

US first quarter GDP growth came in at just 0.1% annualised although this may have been due to bad weather.

Most of the economic indicators out of China such as exports and retail sales continue to show a softer economy than recent years. It should be noted that the pattern has been for the Chinese economy to be soft in the early part of the year and to be stronger in the second half.

A number of emerging market countries that had their currencies sold off earlier in the year (such as Brazil and Indonesia) appear to have stabilized with positive returns in their bond markets this year.

Markets and Economy

A reasonably tough Federal budget means that interest rates are likely to stay low for quite a while in Australia. However the market still expects that the next move in the cash rate will be up and this has contributed to the strength of the Australian dollar.

We are keeping a watch on long term interest rates which have been falling this year. We would have expected rising interest rates given the tapering in the US. However the jury is out on whether or not this is indicating slower future growth which would be bad for equities.

The Australian equity market recently traded at a post GFC high above 5,500 but has pulled back a little since then. In fact global equity markets have done very little this year as most markets are sitting around long term valuation levels. That is to say they are no longer cheap on a PE basis after the rerating we have experienced.

The exception remains emerging market equities although the risks are higher there.

The bottom line is that we would expect equities to outperform fixed interest from current levels but we would not aggressively add to positions right now. This is because we do not believe equity markets will run up quickly from here, but rather drift up if earnings come through as the market expects.

Asset Class	1 month	3 months	1 Year	3 Years	5 Years
Australian Shares	0.29	2.09	13.46	8.54	13.39
Global Shares	-3.02	-2.43	31.10	12.59	11.21
Listed Property	-1.60	3.15	5.02	11.72	15.52
Fixed Interest	0.02	1.45	3.30	6.74	5.95

Federal Budget 2014

The Government delivered a tough budget that was described as the start of a long term repair job. The Government believes that repairing the Budget is necessary to protect living standards and prepare for an ageing population.

Economic impact

The measures announced aim to balance the fine line between repairing the budget and managing the impact of fiscal constraint on economic activity and employment. The budget deficit is forecast to improve substantially starting in the next financial year.

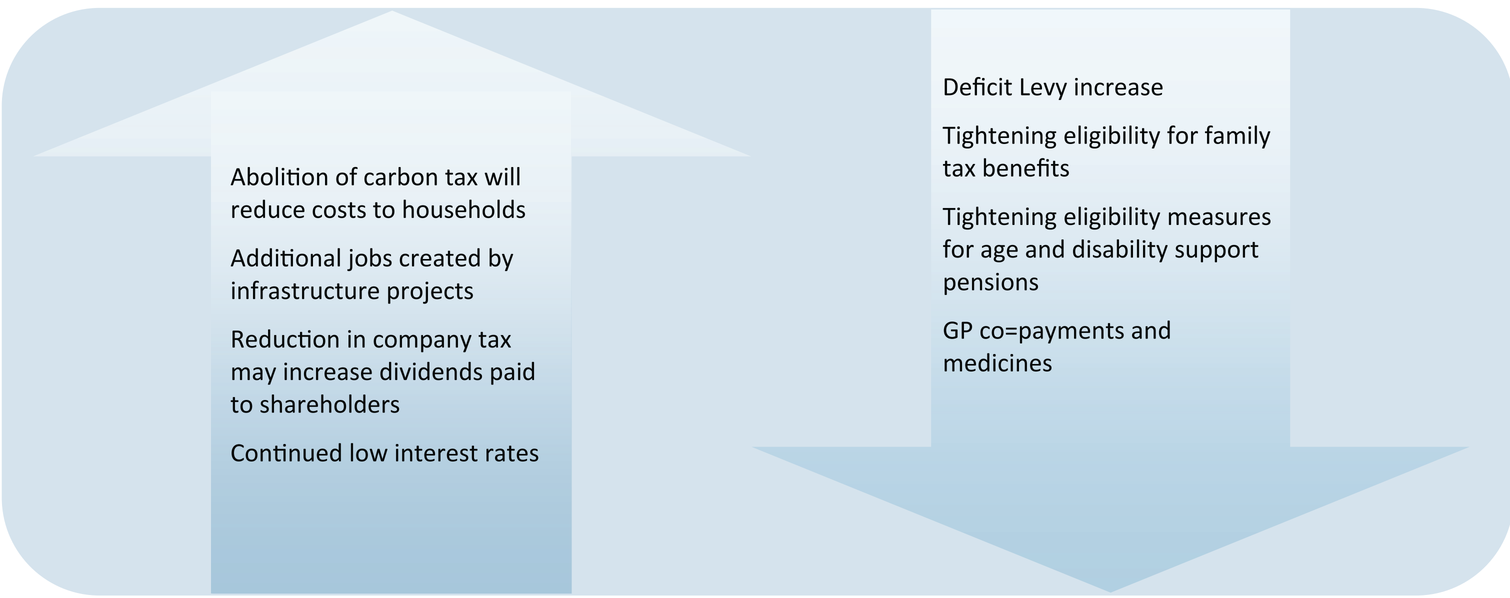
Government debt is forecast to reduce as a result of the reigning in of the deficit. Debt in 2023-24 is projected to be nearly $300 billion lower, even when assuming future tax relief, at $389 billion compared with the $667 billion at the 2013-14 Mid-Year Economic and Fiscal Outlook.

Economic growth is forecast to improve significantly from 3% to 4.75% in 2015/16.

The unemployment rate is forecast to stabilise at 6.25% for the next year and only start to fall below 6% in 2017/18

Consumer spending is likely to be impacted by a number of the announced measures both positively and negatively as illustrated in the diagram below:

The Reserve Bank of Australia is likely to push out any increase in official interest rates until next year at the earliest .



Superannuation

There were no major policy changes to superannuation and a long awaited change to excess concessional contributions is welcomed. Proposed superannuation changes are summarised below:

Refund excess non-concessional contributions
Individuals will be able to withdraw superannuation contributions in excess of the non-concessional contributions cap made from 1 July 2013 and any associated earnings, with these earnings to be taxed at the individual's marginal tax rate.

Super guarantee (SG) increases delayed
The SG rate will increase as legislated from 9.25% to 9.5% from 1 July 2014, and will then increase in 0.5% increments to reach 12% by 1 July 2022.

Financial Year	Proposed SG rate
1 July 2013 – 30 June 2014	9.25%
1 July 2014 – 30 June 2018	9.5%
1 July 2018 – 30 June 2019	10%
1 July 2019 – 30 June 2020	10.5%
1 July 2020 – 30 June 2021	11%
1 July 2021 – 30 June 2022	11.5%
1 July 2022 and later	12%

Taxation

The big headline here was the introduction of the temporary budget repair levy but the applicable income threshold has been increased significantly from early announcements so that it will only impact high income earners on the top marginal tax rate. Proposed taxation changes are summarised below.

Temporary budget repair levy
Commencing 1 July 2014 it is proposed to introduce a 2% levy on taxable income over $180,000. This increases the top marginal tax rate to 49% including the already legislated Medicare levy increase to 2%.

Private health insurance tax offset
The income tier thresholds are proposed to be frozen for three years from 1 July 2015.

Medicare levy surcharge
The Medicare Levy Surcharge thresholds will be frozen for three years from 1 July 2015.

Dependent tax offsets
The dependent spouse tax offset is proposed to be abolished from1 July 2014.
The eligibility income threshold for the dependent (invalid and carer) tax offset is proposed to be reduced from $150,000 to $100,000.

Mature age worker's tax offset
Commencing 1 July 2014 the mature age worker's tax offset is proposed to be abolished for everyone. A subsidy up to $10,000 will be provided to the employer over a two year period to help cover employment costs for each eligible employee.

Medicare levy low income thresholds
The threshold for families is to be increased.

First Home Savers Accounts discontinued
Commencement date: Immediate, but some measures are to be phased in.

Changes for uni students
Several changes are proposed that will affect the cost of university study commencing 1 July 2016.

Social security

Changes have been made to reduce reliance on age pensions and other welfare payments but most changes to pensions will not apply for another three years. The message is clear that clients need to have greater self-reliance to fund a comfortable lifestyle in retirement.

Age pension age
The age pension age is proposed to increase further to age 70 with a full phase-in by 2035. This increase will affect anyone born after 30 June 1958 (currently age 55).

Born between	Eligibility age
Before 1 July 1952	65.5
1 January 1954 - 30 June 1955	66
1 July 1955 - 31 December 1956	66.5
1 January 1957 - 30 June 1958	67
1 July 1958 - 31 December 1959	67.5
1 January 1960 - 30 June 1961	68
1 July 1961 - 31 December 1962	68.5
1 January 1963 - 30 June 1964	69
1 July 1964 - 31 December 1965	69.5
1 January 1966 and later	70

Means-testing threshold freezes
Means-testing changes will reduce access to Centrelink and Veterans' Affairs entitlements over time. But the good news is that homes will not be included in the assets test threshold. Pension changes commence in 2017 while allowance changes commence in 2014

Indexation of pensions

Indexation of Centrelink pensions and the Veterans' Affairs service pension is proposed to be linked only to CPI from 20 September 2017

Disability support pension eligibility review

Recipients of the disability support pension who are under age 35 will need to have a participation plan to ensure those who can move back into the workforce are supported to do so.

Income support bonus abolished

As soon as legislation is passed, the loss of this bonus will see single clients lose $215.60 and couples lose $179.80 each per year.

Impacts for Commonwealth Seniors Health Card

From 1 January 2015 deemed income on account-based pensions will be included in the income definition to test eligibility for the CSHC. Existing cardholders will continue to receive an exemption for account-based pensions commenced before this date. Also eligibility thresholds will index from 20 September 2014 and the Seniors Supplement will be abolished as soon as legislation is passed.

Tougher eligibility for Newstart and Youth allowance

Access to these payments will be restricted with new proposals. Commencing 1 January 2015 for new applicants and 1 July 2015 for existing recipients.

Housing help for seniors – proposal abandoned

Health

GP co-payments

Commencing 1 July 2015, co-payments of $7.00 per visit to a general practitioner (GP) are proposed. $5 of this amount is proposed to be paid into a new Medical Research Future Fund. Concession card holders and children under age 16 will only need to make this co-payment for the first 10 visits in a year – a total of up to $70 per year.

Patients who are not bulk-billed will have their Medicare refund reduced by $5.

The government has also proposed a $5 increase for pharmaceuticals on the PBS scheme, with pensioners paying an additional 80 cents per script.

Families

Paid parental leave (PPL) scheme

A maximum payment of $50,000 over the 26 weeks. Superannuation will also be paid Commencement 1 July 2015

Family tax benefits

Family tax benefit income thresholds will be frozen at current levels for three years from 1 July 2014. The payment rates (excluding supplements) will also be frozen until 30 June 2016. The clean energy supplement is to be renamed the Energy Supplement and because the carbon tax will be abolished, it will not receive any further indexation.

Family Tax Benefit Part B (FTBB) is proposed to be wound back so that it is only paid until the youngest child reaches age six, although families currently eligible may continue to receive the payment until 30 June 2017. To qualify for FTBB the higher income earner (of a couple or the single parent) will need to have income less than $100,000 per annum.

From 1 July 2015, single parents who receive the maximum FTBA and whose youngest child is age six or older may receive a $750 per year payment for each child aged six to twelve.

Schoolkids bonus

This payment will be abolished as soon as legislation is passed. The next payment is due on July 2014. If abolished before then, this payment will not be paid.

Note:
The measures outlined in this paper are all government proposals. The analysis and interpretation is based on information available in the Budget release which is sometimes quite limited. Further details may need to be released to clarify some aspects and legislation needs to be introduced to make the changes effective (unless otherwise indicated). These announcements could be subject to further change before being enacted or may not be implemented.
For more information, please contact your adviser.

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