SEAFG Insights - July 2022

Welcome to our July newsletter and the start of a new financial year. With winter in full swing, it's a great time to rug up by the fire, take stock of the year that was and make plans for the future.

June was a big month in an eventful year for the local and global economy, with inflation and interest rates continuing to dominate. The US Federal Reserve lifted official rates by 0.75% to a target range of 1.50-1.75% to combat surging inflation of 8.6% in the year to May, stoking fears of a US recession.

Australia faces similar but less acute challenges. With inflation sitting at 5.1%, the Reserve Bank lifted the cash rate by 0.5% to 0.85% in June and Governor Philip Lowe hinted at more to come in July. The Australian economy is still growing relatively strongly at an annual rate of 3.3%. Retail trade rose 10.4% in the year to May on the back of low unemployment and high household savings. Household wealth rose to a record high of $574,807 in the year to March, but since then there has been a global sell-off in shares, a slowdown in the Australian housing market and cost of living pressures are mounting. The ANZ-Roy Morgan consumer confidence reading remains weak at 84.7 points (100 is neutral).

Australia's national average petrol price rose to 211.9c a litre in June, the second highest on record, on the back of a surge in global oil prices. Brent Crude rose almost 45% over the past year as the war in Ukraine disrupts supply. Despite a late bounce in shares, the ASX200 fell 9.6% in the year to June, while US shares were down more than 12%. The Aussie dollar lost ground over the financial year to finish below US69c.

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A SUPER WINDOW OF OPPORTUNITY

New rules coming into force on July 1 will create opportunities for older Australians to boost their retirement savings and younger Australians to build a home deposit, all within the tax-efficient superannuation system.

Using the existing First Home Super Saver Scheme, people can now release up to $50,000 from their super account for a first home deposit, up from $30,000 previously.

Another change that will help low-income earners and people who work in the gig economy is the scrapping of the Super Guarantee (SG) threshold. Previously, employees only began receiving compulsory SG payments from their employer once they earned $450 a month.

But the biggest potential benefits from the recent changes will flow to Australians aged 55 and older. Here's a rundown of the key changes and potential strategies.

Work test changes

From July 1, anyone under the age of 75 can make and receive personal or salary sacrifice super contributions without having to satisfy a work test. Annual contribution limits still apply and personal contributions for which you claim a tax deduction are still not allowed.

Previously, people aged 67 to 74 were required to work for at least 40 hours in a consecutive 30-day period in a financial year or be eligible for the work test exemption.

This means you can potentially top up your super account until you turn 75 (or no later than 28 days after the end of the month you turn 75). It also opens potential new strategies for a making big last-minute contribution using the bring-forward rule.

Extension of the bring-forward rule

The bring-forward rule allows eligible people to "bring forward" up to two years' worth of non-concessional (after tax) super contributions. The current annual non-concessional contributions cap is $110,000, which means you can potentially contribute up to $330,000.

When combined with the removal of the work test for people aged 67-75, this opens a 10-year window of opportunity for older Australians to boost their super even as they draw down retirement income.

Some potential strategies you might consider are:

- Transferring wealth you hold outside super – such as shares, investment property or an inheritance – into super to take advantage of the tax-free environment of super in retirement phase
- Withdrawing a lump sum from your super and recontributing it to your spouse's super, to make the most of your combined super under the existing limits
- Using the bring-forward rule in conjunction with downsizer contributions when you sell your family home.

Downsizer contributions age lowered to 60

From July 1, you can make a downsizer contribution into super from age 60, down from 65 previously. (In the May 2022 election campaign, the previous Morrison government proposed lowering the eligibility age further to 55, a promise matched by Labor. This is yet to be legislated.)

The downsizer rules allow eligible individuals to contribute up to $300,000 from the sale of their home into super. Couples can contribute up to this amount each, up to a combined $600,000. You must have owned the home for at least 10 years.

Downsizer contributions don't count towards your concessional or non-concessional caps. And as there is no work test or age limit, downsizer contributions provide a lot of flexibility for older Australians to manage their financial resources in retirement.

For instance, you could sell your home and make a downsizer contribution of up to $300,000 combined with bringing forward non-concessional contributions of up to $330,000. This would allow an individual to potentially boost their super by up to $630,000, while couples could contribute up to a combined $1,260,000.

Rules relaxed, not removed

The latest rule changes will make it easier for many Australians to build and manage their retirement savings within the concessional tax environment of super. But those generous tax concessions still have their limits.

Currently, there's a $1.7 million limit on the amount you can transfer into the pension phase of super, called your transfer balance cap. Just to confuse matters, there's also a cap on the total amount you can have in super (your total super balance) to be eligible for a range of non-concessional contributions.

As you can see, it's complicated. So if you would like to discuss how the new super rules might benefit you, please get in touch.

Source: ATO

A WILL TO give

As baby boomers shift into retirement, Australia is on the brink of the nation's biggest ever intergenerational wealth transfer. Yet estate or inheritance planning is rarely discussed by families.

Talking openly about how you want your assets to be passed on can help avoid family disputes that take a toll both financially and emotionally. It provides a certain peace of mind for you – that your intentions will be met – and for your family and friends.

Certainly the stakes have never been higher, with growing house prices and healthy superannuation balances contributing to a considerable increase in the wealth of many older Australians in the past two decades.

Around $1.5 trillion was transferred in gifts or inheritances between 2002 and 2018. In 2018 alone, some $107 billion dollars was inherited while $14 billion was handed out in gifts.[i]

The importance of planning

With so much at stake, having an estate plan in place helps to protect the interests of those you care about and to fulfil your wishes. It takes careful thought and professional advice, but that is no excuse for putting the task aside for later. If something happens to you in the meantime, your assets may not be distributed as you would like and there could be tax implications for your beneficiaries.

An estate plan includes a Will and, in some cases, funeral arrangements and instructions for the care of children and animals. Without a Will, your assets will be distributed according to state inheritance laws which may not be what you intended.

A plan may also include instructions for a testamentary trust to hold assets that are then distributed in a tax-effective way to your beneficiaries. And don't forget your 'digital will', a list of any online accounts and passwords that may be important.

Meanwhile, to protect your interests in case you are incapacitated in some way, an enduring power of attorney and a medical power of attorney nominate the people you would like to handle your affairs until you are better.

Complex families

Estate planning is even more important in the case of blended families or for those with complex family relationships, especially where the emotional issue of the family home is concerned.

Disputes often centre around who gets the house when there are children from a previous marriage, but your new spouse is living in the family home. You could allocate other assets to the children and leave the home to your spouse or require that the house be sold and the proceeds distributed to all. Alternatively, your Will could grant lifetime tenure in the home for your spouse with it passing to your children after your spouse dies. Having conversations early about your intentions, can help alleviate possible conflict.

If you are concerned about protecting the interests of a family member with mental health or addiction issues, a testamentary trust can help to look after your assets and distribute funds in a controlled way. A testamentary trust is also often used to provide for young children, holding the assets until they reach adulthood.

Dividing it up

When it comes to deciding how best to allocate assets among children, some prefer to hand out equal shares no matter their individual financial circumstances, while others prefer to give extra to one who may be struggling. Given that Wills are frequently challenged by family members or others who believe they are owed a share or an even bigger share, it's wise to make your intentions clear in your Will including reasons and documentation.

While people who receive inheritances are usually well into middle age – on average 50-years-old[ii] – and perhaps comfortably well-off, you could choose to bypass the next generation. Instead, you might consider leaving your estate to grandchildren, to help set them up with a deposit for a home or covering school fees.

Another option is to begin distributing your estate while you are alive and can share the enjoyment of the benefits the extra financial help might bring.

What's not covered?

It is important to note that some assets are not covered by your Will. These include assets jointly held with someone else (such as a bank account or a house), super benefits and life insurance.

In the case of jointly held assets, ownership generally passes to the surviving partner and life insurance is paid to the beneficiary named in the policy. For super, it's vital to complete a binding death benefit nomination to ensure the funds are paid to the person you choose.

With so much to consider, expert advice is critical when preparing an estate plan, so call us to begin the discussion.

i https://www.pc.gov.au/research/completed/wealth-transfers

ii Wealth Transfers and their Economic Effects - Commission Research Paper - Productivity Commission (pc.gov.au)

YOUR INVESTING STYLE

– as unique as you

As interest rates start to increase after a lengthy period of historical lows, it's a good time to think about how your money is working for you and whether your investing style and strategy is still in line with your goals.

Higher interest rates don't just send a ripple through the economy, aside from the obvious impact on the property market, they often impact stock prices. There are a myriad of other factors that contribute to market movement and portfolio performance and trying to navigate all the things that need to be considered can be challenging but being aware of your preferred investment style and having a considered and appropriate strategy can help.

The benefits of style and strategy

Just as we are all unique individuals, our goals and approach to investing will also be different to our family and friends and it pays to be familiar with your own style and preferences.

It can be common for those new to investing to take the plunge without any real plan, let alone an investment strategy that's likely to align with their current circumstances, future requirements, and investment goals.

Even those who have been investing for some time can be guilty of a 'set and forget' approach that might mean hanging on to a strategy that does not meet their present or future needs.

Having the right investment strategy – the one that's right for you – improves the likelihood of your investments meeting your goals and allows you to sleep at night.

Your tolerance for risk at the core of your style

While approaches to, and styles of investing are many and varied, your comfort with risk is often the primary driver of any approach you may choose to take. There is of course a trade-off between risk and return that needs to also be considered. Your comfort with risk will determine the right mix of asset classes in your portfolio.

An aggressive investor, commonly someone with higher risk tolerance, is willing to take on greater risk for the possibility of better returns than a conservative investor. This type of investor will be comfortable with a higher proportion of growth assets like shares or listed property that offer higher returns over the long-term that may come at the expense of less stable returns.

A conservative investor will employ a larger proportion of defensive assets in their portfolio to provide long-term stable returns with lower volatility and exposure to risk. Defensive assets are fixed interest investment options including fixed income bonds and cash investment options.

Hands-on vs hands-off approach

Investing strategies can be further separated into two distinct groups: active and passive.

Passive investing, as the name implies, focuses on benefitting from the overall increase in market prices over time. One of the benefits of passive investing is that it minimises the mistakes investors can make when they react emotionally to stock market movement.

Active investing involves a more hands-on approach, with more frequent buying and selling to take advantage of short-term price fluctuations and is generally undertaken by a portfolio manager.

Changing your strategy over time

Most investors find that their investment style shifts as they age. Younger investors have a longer time horizon, so they may feel more comfortable making riskier investments as they have time for the market to recover from market falls. Mature investors may be more focused on preserving their savings for retirement, so they may be more interested in diversification and dollar-cost averaging.

For investors nearing or at retirement, a shift from asset growth and capital gains to a focus on income may be something worth considering and is often desired. The advantage of an income focussed strategy is that investments can produce some of the cash flows needed when you're no longer working. Dividend stocks are a common way to achieve this goal, with companies showing stable and growing dividends providing the most value.

To ensure you are employing the right strategy to meet your objectives, it pays to be aware of your options and revisit your comfort with risk and your overall investment goals. We can ensure your investment portfolio meets both these elements throughout your various life stages.

If you are interested in exploring the options available to you, please get in touch. We can work closely with you to review your strategy or if you are new to investing, find the right mix for your unique circumstances.