Newsletter: June 2020

Welcome to the latest edition of our client newsletters.

Our articles cover a range of topics which we hope you will find interesting. We aim to keep you informed of changes as they happen, but we also want to provide ideas to help you live the life you want – now and in the future.

In this edition topics include:

- Investment options and retirement
- Checklist for the end of financial year
- The Australian economy and recovery from COVID-19.

If you would like to discuss any of the issues raised in this newsletter, please don't hesitate to contact us.

In the meantime stay warm and we hope you enjoy the read.

All the best

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Investment options and retirement

If retirement was on your horizon in the next five years or so, the market downturn due to COVID-19 coronavirus might have prompted you to take a closer look at your superannuation and how it's invested. Perhaps you've seen your balance drop and are now wondering what you need to do to get your retirement back on track?

In this article, we explain, generally, what super funds do with retirement savings, the different types of investment options to choose from, stage of life considerations, and the implications of changing investments.

What super funds do with your money?

Generally, no less than 9.5% of your before-tax salary (if you're eligible) is paid into super by your employer, which is then taxed at a maximum of 15%. Or if you are self-employed, the amount you've paid into your super, if you've chosen to invest in one, will be at your discretion. A super fund will then invest this money over the course of a person's working life, so they can hopefully retire comfortably.

A person can choose from a range of investment options and generally the main difference will be the level of risk they're willing to accept to have the potential opportunity to generate higher returns. There are never guarantees of higher returns and it's important to understand the risks and returns before you make a decision about what suits your appetite and circumstances.

Super investment options you can choose from

Most super funds let you choose from a range or mix of investment options and asset classes. These might include 'growth', 'conservative' and 'cash' but the terms can differ across super funds. Here's a small sample of the typical type of investment options available:

Growth options aim for higher returns over the long term, however losses can also be notable when markets aren't performing. This option generally invests around 85% in shares or property.

Balanced options try to have a mix of asset investment which may impact the overall return. Generally, during a market downturn, any losses experienced may be lower. This option typically invests around 70% in shares or property, with the rest in fixed interest and cash.

Conservative options generally aim to reduce the risk of market volatility and may generate lower returns. It typically invests approx. 30% in shares and property, with the rest in fixed interest and cash.

Cash options aim to generate stable returns. It typically invests 100% in deposits with Australian deposit-taking institutions, such as banks, building societies and credit unions.

Super funds may have different allocations, so it's important to read your super fund's product disclosure statement in full.

How your stage of life may influence your preference

Choosing the most suitable investment option generally may come down to one's goals for retirement, their attitude to risk and the time a person has available to invest.

As a person gets closer to retirement, they may prefer a more conservative approach to investing as a share market crash can be harder to recover from.

However, if someone is five years or less from retiring, it's important to understand the impacts any changes to an investment option may have on a retirement outcome.

Implications of changing investment options

People should think carefully before deciding to change investment options and if possible, speak to us to understand the implications before making a decision.

For example, if you've seen your super balance go down and are thinking about changing your investment option, say from a balanced fund to a conservative or cash fund, this may see you lock in any losses. It's similar to selling a house at the bottom of a market slump – most people would think twice and consider allowing the property market time to bounce back before taking that step.

It's not just locking in your losses to think about. Depending on the type of fund you have, there may be capital gains tax (CGT) or other tax/fee implications when switching investment options.

It's important to remember that the decisions you make about your retirement savings at this stage in your life could potentially mean the difference between a comfortable and not-so-comfortable retirement.

If you need further help in making sure your retirement's on track, speak to us.

We can bring the right knowledge, expertise and guidance to identify your specific goals, and help you achieve them.

Checklist for the end of financial year

The end of financial year on 30 June is a good time to take stock and get your finances in order.

This is an end of financial year like no other.

Being prepared, reviewing your super contributions and submitting your return on time are good policies every year, but the shadow of COVID-19 (coronavirus) means many of us face unexpected pressures in a changing economic environment.

Many people will have concerns around job security, which makes long-term planning seem less important.

You may face urgent priorities for your money, such as mortgage repayments, covering bills and paying down debt.

If you've worked from home this year, the government has recently released guidance on claiming working from home expenses as a tax deduction. Due to COVID-19, this financial year the ATO will accept a shortcut method for calculating running expenses from 1 March to 30 June.

Here are some other things to consider as 30 June approaches.

What's new this year if you're at or near retirement

Changes kicking in this financial year include lower minimum pension drawdown requirements to help retirees affected by significant losses in financial markets as a result of COVID-19.

The minimum annual payment required for account-based and allocated pensions and annuities has been cut by 50% in the 2019–20 and the 2020–21 financial years.

If you've recently retired, you may still be able to make voluntary super contributions and potentially claim a tax deduction for personal super contributions. Current regulations allow eligible 'recent' retirees, aged 65 and over, a limited exemption from having to meet the work test, which is otherwise required to make voluntary super contributions. This applies to contributions made from 1 July 2019.

This is also the first year that those who are eligible can use unused carried forward concession cap amounts from the previous financial year.

First applications for early release of super withdrawals up to $10,000 must be made by 30 June. A further application can be made between 1 July and 24 September 2020.

Super fund members born between 1 July 1962 and 30 June 1963 will reach their preservation age during the 2020/21 financial year and may wish to consider whether a transition to retirement pension is appropriate.

Proposed changes

From 1 July 2020, the following proposed changes, if legislated, may benefit members aged 65 and 66 who want to make additional contributions to super. Note that legislation around these changes hasn't yet been passed.

- Up to age 67 (currently 65) you will be able to make personal and non-mandated employer contributions to super without needing to satisfy the work test (ie been gainfully employed for 40 hours in 30 consecutive days during the financial year in which the contributions are made).
- You will be able to access the bring forward provisions for the non-concessional cap up to age 67 (currently 65). This means you will be able to contribute up to $300,000 to super (you can generally bring forward up to $300,000 if your total super balance on the previous 30 June is less than $1.4m, or up to $200,000 if it's less than $1.5m).
- The maximum age at which you will be able to receive a spouse contribution will increase from 70 to 74.

Think about making extra super contributions

End of the financial year is usually a good time to think about making extra contributions to take advantage of the lower rates of taxation on super.

While that might be harder this year with competing priorities, it still makes sense to keep in mind that additional contributions today could boost your super balance in the future. There are a number of different types of contributions to consider. You may also be able to reduce your taxable income and pay less on investment earnings.

To claim a tax deduction on your post tax contributions, you need to tell your super fund by filing a notice of intent. You will generally need to lodge this notice, and have the lodgement acknowledged by your fund, before you file a tax return in the year you made the contributions.

If you're earning more than your partner and would like to top up their retirement savings, or vice versa, you may want to think about spousal contributions. The spouse making the spousal contributions could be eligible for a tax break.

You and/or your partner may also be eligible to receive a government co-contribution. If so, you might consider making a personal non-concessional contribution before 30 June to make sure you receive the matching government co-contribution for the 2019-20 financial year that you are entitled to.

Consider your insurance premiums

If you have income protection cover, and your budget allows, you may consider pre-paying your premiums 12 months in advance to take advantage of claiming a bigger tax deduction this year. This may work well if your income is higher in the current income year than next.

However, it is important to get some tax advice as to whether doing so this year is a good idea for you based on your income.

Talk to a professional

If you use a tax agent to complete your return, it's worth having a word with them about your circumstances to see if there are other potential savings you can make. Also have a word with us, if you haven't already as we can assist you to make the best decisions for your situation at this time.

The Australian economy and recovery from COVID-19

Dr Shane Oliver - Head of Investment Strategy and Economics and Chief Economist, AMP Capital

The shutdown in response to COVID-19 (coronavirus) has wreaked havoc on the economy, but after a period of free-fall we could be beginning to see light at the end of the tunnel.

What has the impact been on consumer confidence and spending?

Consumer confidence collapsed due to uncertainty around how long the economic shutdown would last, what the damage would be, how great the health threat was and what it would mean for wages and jobs. But confidence has since recovered a bit.

Despite an initial boom in retail spending due to stockpiling of groceries, toilet paper and home office supplies, shopping centres are now deserted, so retail sales are probably down by around 20%, although online sales appear to be a bright spot.

How similar (or different) is this to other financial crises in recent history?

In terms of the shrinking Australian economy, as measured by gross domestic product (GDP) and rising unemployment, this is going to look most like the Great Depression of the 1930s. However, that was a boom then bust scenario, so this doesn't really resemble anything we've seen in the past 100 years. Once the shutdowns are eased, economic conditions should bounce back far quicker than they did after the Great Depression or after past recessions.

What impact is the relaxing of isolation rules in some parts of Australia having?

It's very positive news that the shutdown, which we were originally told might last at least six months, may now only last for two months, and is part of the reason consumer confidence has picked up a bit lately. While so far, the easing of rules has been more related to social interactions and freedom of movement, we expect other, more economically significant easing will occur in the coming weeks.

What long-term impact will the government stimulus packages have on the Australian economy?

The long-term cost is that our level of public debt relative to the economy will double, so either we accept a much higher level of public debt or we try and pay it down – to do that the government will either raise taxes or cut spending. But if the government had stood by and done nothing, we'd have much higher unemployment and the hit to economic activity would last for much longer. And our level of public debt is starting from a much lower level than in the US, Europe or Japan.

What impact will other factors such as the fall in oil prices and the fall in value of the Australian dollar have on our economic recovery?

So far, the fall in the oil price has been seen as a negative due to the impacts on large oil producers. But once the lockdowns are eased and we're driving around again it will be positive as Australian households could be saving up to $25 a week on petrol. Historically, lower oil prices have gone hand-in-hand with low interest rates to fuel economic recovery – and interest rates in Australia are unlikely to rise for the next three to four years.

The Australian dollar started the year at 70 cents against the US$, fell to a low of 55 cents and is now around 64 cents, but that will help the economy. It makes our exports more competitive internationally and is particularly good for our natural resources exporters who get paid in US$.

What will the impact of COVID-19 be on Australian house prices?

House price growth has slowed down and listings have dried up due to the uncertainty. The JobKeeper payments introduced by the Federal Government and loan repayment holidays offered by the banks have delayed the hit to the property market, but with unemployment heading higher, there will be some distressed sales and impact on prices.

It will depend on how quickly the economy recovers after the six-month stimulus and mortgage payment freeze period ends as to whether we see a 5-10% hit to house prices or whether it's more like 20%. Our base case is for a 10% fall assuming a return to economic growth through the second half of the year.

Will the economy, or the way we work, be permanently changed as a result of the current downturn?

It's unlikely bans on international travel (except to NZ) will be lifted before there's a vaccine, which will affect airlines, accommodation providers and tour operators. However, the impact will be cushioned by a rise in domestic travel as Australians holiday at home. In fact, we have a tourism trade deficit with the rest of the world, so the absence of international travel will benefit Australian GDP (in the short term).

Work-related travel may also be permanently affected, as businesses are now using technology to effectively communicate with interstate and overseas offices. Work from home arrangements are also likely to be more widely embraced affecting demand for office space but reducing traffic congestion.

Retail may be permanently damaged as the shift away from bricks and mortar retailers to online retail has been accelerated, and universities that rely on international students may struggle for a while yet.

There's also talk of reforms to help the economy grow faster. This could include things such as tax reforms, improving the industrial relations system and reducing regulation to make it easier for companies to start and operate.

How long will the Australian economy take to recover?

We at AMP Capital predict that the high point for Australian economic activity as measured by GDP looks to have been the last quarter of 2019 and it's projected to shrink 10-15% by the middle of 2020. But once workplaces are able to start re-opening, which is likely from this month onwards, economic activity will pick up and growth will occur through the second half of 2020. It will probably take about 18 months to get back to our recent highs, so a full recovery is unlikely before the end of 2021.

Unemployment was 5.2% in March and will probably be around 10% by mid-2020. It will take longer to fall as some companies will use the current crisis as an opportunity to cut their costs, and by the end of 2021 it will probably be around 7%.