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July 2021

It's July, there's a nip in the air and winter has well and truly set in, as Australia deals with COVID outbreaks across several states. But July also marks the start of the new financial year, a good time to reflect on how far we have come since this time last year and to make plans for the year ahead.

As the financial year ended, there was plenty to celebrate on the economic front despite the continuing impact of COVID-19. Australia rebounded out of recession, with economic growth up 1.8% in March, the third consecutive quarterly rise. Interest rates remain at an historic low of 0.1% and inflation sits at just 1.1%, well below the Reserve Bank's 2-3% target. Despite fears that global economic recovery will lead to higher inflation and interest rates, the Reserve has indicated rates will not rise until 2024 or annual wage growth reaches 3% (currently 1.5%).

In other positive news, unemployment continues to fall - from 5.5% to 5.1% in May. Retail trade rose 0.1% in May, up 7.4% up on the year, as consumer confidence grows. The ANZ-Roy Morgan consumer confidence index lifted by almost a point in June to 112.2 points.

Australia's trade surplus increased from $5.8 billion in March to $8 billion in April, the 40th consecutive monthly rise, on the back of strong Chinese demand for our iron ore and other commodities. Iron ore prices rose 6.7% in June and almost 36% in 2021 to date. Oil prices have also surged, with Bent Crude up 8.4% in June and 45% this year. That's good for producers and energy stocks, but not so good for businesses reliant on fuel and consumers at the petrol bowser. The Aussie dollar finished the year around US75c, up from US69c a year ago but down on its 3-year high of just under US80c in February due to US dollar strength.

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The NEW Financial Year rings in SUPER CHANGES

As the new financial year gets underway, there are some big changes to superannuation that could add up to a welcome lift in your retirement savings.

Some, like the rise in the Superannuation Guarantee (SG), will happen automatically so you won't need to lift a finger. Others, like higher contribution caps, may require some planning to get the full benefit.

Here's a summary of the changes starting from 1 July 2021.

Increase in the Super Guarantee

If you are an employee, the amount your employer contributes to your super fund has just increased to 10 per cent of your pre-tax ordinary time earnings, up from 9.5 per cent. For higher income earners, employers are not required to pay the SG on amounts you earn above $58,920 per quarter (up from $57,090 in 2020-21).

Say you earn $100,000 a year before tax. In the 2021-22 financial year your employer is required to contribute $10,000 into your super account, up from $9,500 last financial year. For younger members especially, that could add up to a substantial increase in your retirement savings once time and compound earnings weave their magic.

The SG rate is scheduled to rise again to 10.5 per cent on 1 July 2022 and gradually increase until it reaches 12% on 1 July 2025.

Higher contributions caps

The annual limits on the amount you can contribute to super have also been lifted, for the first time in four years.

The concessional (before tax) contributions cap has increased from $25,000 a year to $27,500. These contributions include SG payments from your employer as well as any salary sacrifice arrangements you have in place and personal contributions you claim a tax deduction for.

At the same time, the cap on non-concessional (after tax) contributions has gone up from $100,000 to $110,000. This means the amount you can contribute under a bring-forward arrangement has also increased, provided you are eligible.

Under the bring-forward rule, you can put up to three years' non-concessional contributions into your super in a single financial year. So this year, if eligible, you could potentially contribute up to $330,000 this way (3 x $110,000), up from $300,000 previously. This is a useful strategy if you receive a windfall and want to use some of it to boost your retirement savings.

More generous Total Super Balance and Transfer Balance Cap

Super remains the most tax-efficient savings vehicle in the land, but there are limits to how much you can squirrel away in super for your retirement. These limits, however, have just become a little more generous.

The Total Super Balance (TSB) threshold which determines whether you can make non-concessional (after-tax) contributions in a financial year is assessed at 30 June of the previous financial year. The TSB at which no non-concessional contributions can be made this financial year will increase to $1.7 million from $1.6 million.

Just to confuse matters, the same limit applies to the amount you can transfer from your accumulation account into a retirement phase super pension. This is known as the Transfer Balance Cap (TBC), and it has also just increased to $1.7 million from $1.6 million.

If you retired and started a super pension before July 1 this year, your TBC may be less than $1.7 million and you may not be able to take full advantage of the increased TBC. The rules are complex, so get in touch if you would like to discuss your situation.

Reduction in minimum pension drawdowns extended

In response to record low interest rates and volatile investment markets, the government has extended the temporary 50 per cent reduction in minimum pension drawdowns until 30 June 2022.

Retirees with certain super pensions and annuities are required to withdraw a minimum percentage of their account balance each year. Due to the impact of the pandemic on retiree finances, the minimum withdrawal amounts were also halved for the 2019-20 and 2020-21 financial years.

Time to prepare

There's a lot for super fund members to digest. SMSF trustees in particular will need to ensure they document changes that affect any of the members in their fund. But these latest changes also present retirement planning opportunities.

Whatever your situation, if you would like to discuss how to make the most of the new rules, please get in touch.

Go for gold to achieve your goals

The Olympic Games always provides a platform to marvel at what humans are capable of, as the athletes competing strive to be the fastest, the strongest or just the best, to win gold. While this year may be a little different, the Games still give us the opportunity to be inspired by the remarkable performances of the athletes as they compete.

The passion and discipline in perfecting their craft has propelled these athletes to elite level, so it's not surprising that many have also found success outside the sporting arena by transferring this focus to new endeavours.

So how can we apply the same determination and focus to achieving success in our everyday lives?

Set clear, realistic goals

SMART (Specific, Measurable, Attainable, Relevant and Time-Bound) goals are commonly used by athletes to get closer to their medal dreams.[i] By following this structure, your goals will become clearer and will more likely lead you to where you want to go.

No athlete has reached gold by loftily thinking they '*might* train today'! They have a well-planned schedule and overall plan to develop their skills and abilities to elite level. You can do so in other facets of your life as well through goal setting – and then following through.

Build a great team to support your efforts

While we are focused on the athlete, there is an entire team of people behind their success. Usually from a young age, their parents ferried them around, coaches imparted their wisdom and fellow athletes helped improve their skills through competition. Then there are the trainers, physios, dietitians and life coaches who make up a champion's team.

While you may not need to assemble an entourage, building a strong network can support your endeavours, keep you accountable and provide ongoing motivation. Perhaps this is an advisor or mentor, a business coach, a career specialist, or perhaps even a savvy friend or family member. Get them on board by sharing your vision and outlining how they can help.

Play to your strengths

While there are some athletes who have won Olympic medals in different sports, the majority specialise in one area.[ii] By playing to your strengths, you can dedicate your time and energy to a set goal, honing your skills and building on an already strong foundation without overextending yourself.

A much-loved story in Olympic history that illustrates playing to strengths is that of Australian speed skater Steven Bradbury. Realising he was not the fastest skater in the group, Steven's tactic was to stay back of the pack to avoid a collision, which had happened in an earlier race trial. His smarts (and good luck!) paid off when the faster skaters collided, leaving Steven to cross the finish line and win gold.[iii]

Project confidence

"I am the greatest; I said that even before I knew I was," boxer Muhammad Ali famously stated. While we don't all have Ali-levels of confidence, we can take a note from his book in projecting an air of confidence.

This may require a bit of a 'fake it 'til you make it' approach, but it won't be long until this transforms into actual self-belief. Studies have found that adjustments we make to our bodies, such as standing up straight and smiling, can result in improved mood.[iv]

Embrace failure

No-one likes failing, especially those of us who are competitive. Yet athletes learn from failure, using it to improve and craft their skills, inching towards success.

Failure also builds resilience, by dusting yourself off and not giving up, you develop the tenacity to keep going when times are tough. Use failure as a learning experience that helps you grow, develop and take steps towards your ultimate goal.

As we watch the world's best athletes perform in Tokyo, be inspired to dream big and set your own goals, making sure you then follow through to achieve your very own version of success.

i https://www.forbes.com/sites/davidcarlin/2020/01/10/why-olympic-athletes-are-smarter-than-you/?sh=77bd0d667384

ii https://en.wikipedia.org/wiki/List_of_athletes_with_Olympic_medals_in_different_sports

iii https://www.youtube.com/watch?v=fAADWfJO2qM

iv https://psychcentral.com/blog/fake-it-till-you-make-it-5-cheats-from-neuroscience#1

WHAT'S UP WITH INFLATION?

Fears of a resurgence in inflation has been the big topic of conversation among bond and sharemarket commentators lately, which may come as a surprise to many given that our rate of inflation is just 1.1 per cent. Yet despite market rumblings, the Reserve Bank appears quite comfortable about the outlook.

Inflation is a symptom of rising consumer prices, measured in Australia by the Consumer Price Index (CPI). The RBA has an inflation target of 2-3 per cent a year, which it regards as a level to achieve its goals of price stability, full employment and prosperity for Australia.

Currently the RBA expects inflation to be 1.5 per cent this year in Australia, rising to 2 per cent by mid-2023.[i] Until the inflation rate returns to the 2-3 per cent mark, the RBA has said it will not lift the cash rate.

US inflation rising

The situation is a little different overseas where inflation has spiked higher. For instance, US inflation shot up to an annual rate of 5 per cent in May, the fastest pace since 2008, up from 4.2 per cent in April.[ii] As experienced investors would be aware, markets hate surprises. So with inflation rising faster than anticipated, share and bond markets are on edge.

But just like the RBA, the Federal Reserve views this spike as temporary, pointing to its being a natural reaction after the fall in prices last year during the worst days of the COVID crisis. In addition, companies underestimated demand for their goods during the pandemic and as a result there are now bottlenecks in supply that are putting upward pressure on prices.

The central banks believe that once economies get over the kickstart from all the government stimulation, inflation will fall back into line. After all, most world economies went backwards last year, so any growth should be viewed as a good thing and more than likely a temporary event.

But markets are not convinced.

Inflation and wages

Market pundits argue that if businesses must pay more for materials and running costs such as electricity then these increases will most likely be passed on to the consumer.

That's all very well if your wages also rise, but if your income remains static then your standard of living will go backwards as you will have to spend more money to buy the same goods.

This then becomes a vicious circle. If the cost of living rises, then you will seek higher wages; this will the put further pressure on the costs for businesses. They will then have to increase their prices further to cover the higher wages bill. Some companies may react by reducing staff levels which will lead to higher unemployment.

Impact on investment

Inflation can also have a negative impact on investors because it reduces their real rate of return. That is, the gross return on an investment minus the rate of inflation.

Rising prices and interest rates also impact company profits. With companies facing higher costs, the outlook for corporate earnings growth comes under pressure.

But not all stocks are affected the same. Companies that produce food and other essentials are not as sensitive to inflation because we all need to eat. Mining companies also benefit from rising prices for the commodities they produce. Whereas high growth stocks like technology companies traditionally suffer from rising interest rates.

Markets current fear is that central banks will tighten monetary policy faster than expected. Interest rates will rise, money will tighten, and this will fuel higher inflation.

Bond market fallout

Expectations of higher inflation has already seen the bond market react, with the 10-year bond yield in both Australia and the US on the rise since October last year.

If yields rise, then the value of bonds actually fall. This is particularly concerning for fixed income investors. Not only are you faced with the prospect of capital losses because the price of your existing bond holdings generally falls when rates rise, but the purchasing power of your income will also be reduced as inflation takes its toll. Investments in inflation-linked bonds should fare better in an inflationary environment.

Inflation is part of the economic cycle. Keeping it under control is the key to a well-run economy and that is where central banks play their role.

Call us if you would like to discuss how an uptick in inflation may be impacting your overall investment strategy.

i https://www.rba.gov.au/media-releases/2021/mr-21-09.html

ii https://tradingeconomics.com/united-states/inflation-cpi