May Newsletter

The Budget and Investment outlook. 2018-19

The Budget:

Many of you have probably absorbed as much as you want about the budget.

This is my quick summary:

- From a Financial Planning perspective there is no significant changes that require tweaking of strategies or longer term plans. There was not a lot that raised issues or concerns.
  Although it is obviously an election budget – no real nasty surprises.
- The tax rate – if it gets through Parliament will stretch out the 32.5% tax band from a limit of $87,000 to $90,000 in the next financial year and then further in the future.
  In 2022 (4 years away they will also stretch the 19% tax limit from $37,000 to $41,000).
- Small businesses get an extension of the immediate $20,000 tax write-off for major capital purchases.
- The one area of interest perhaps to some – was that the Government has decided to expand their own "Reverse Mortgage" arrangements, which were previously under the counter offers. "The Pensions Loan scheme" allows a higher age pension rate in exchange for equity in the pensioner's house. It has been previously little used. The applicant must be receiving an age pension and can lift the payments up to 50% of the full age pension that they would be entitled to. The interest rate is lower than commercially provided reverse mortgages. However, as in all cases the capitalisation of the interest means that a suitable time limit should be chosen, say 10 years before the home is sold and the debt repaid.

  This expansion of the scheme has been criticised as a counterproductive move which inhibits the intent of the downsizing legislation also just passed. But it offers flexibility to many older citizens.

Many other changes that do not have an impact on day to day lives are also proposed from July 2019.

Given the current makeup of the parliament they may not get through.
Legislation could be blocked or varied under negotiations.

- Westpac's chief Economist Bill Evans (who has a great track record on picking inflation and RBA interest rate moves) has given the budget a cautious thumbs up, and sees the next 2 years forecasts by Treasury in line with his and Westpac's. The economy has had a good 18 months and the deficit will reduce while tax cuts are also handed out. He does acknowledge that the forecast beyond that are optimistic – but the global synchronised upswing may justify those.
- Ross Gittins from the Sydney Morning Herald however, sees the budget as a bit of tricky dick accounting. Using long forecast forward estimates to justify the outcome, with only 10% of the costs (Tax cuts etc.) hitting home in the first 12 months – the rest is promised in the future. He has a point, who can remember what the promises of past budgets are – have they been delivered?

What was the average person supposed to be earning / taxed / receiving in government benefits in 2018 from the 2013 budget …?? Anyone?

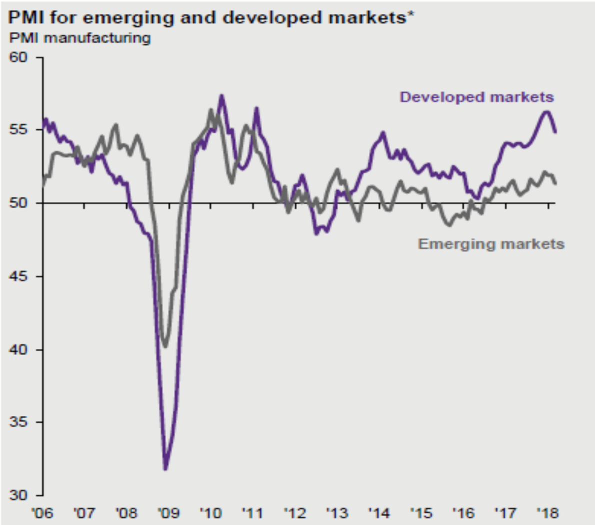
Global Economy:

This now leads me to raise the outlook for the Australian and Global economy.

Last November we outlined a positive view of the synchronised global upswing.

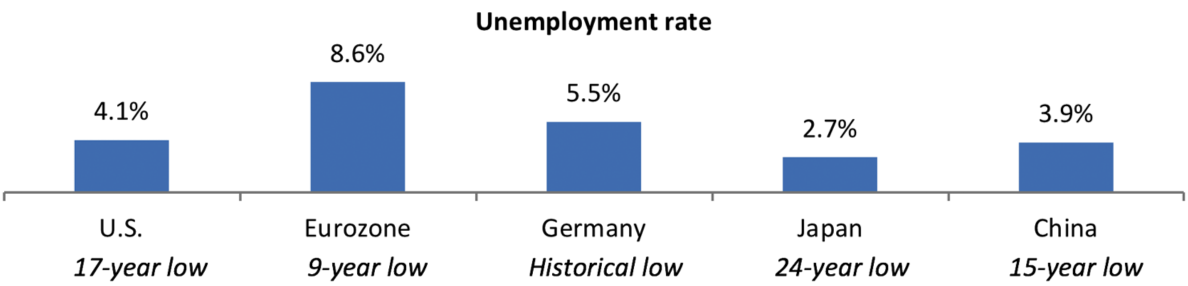
6 months on there is no change to that 2 year view, with a few charts here to show the more recent figures to reinforce the trend.

The first shows global manufacturing over 12 years and its accelerating growth and activity.



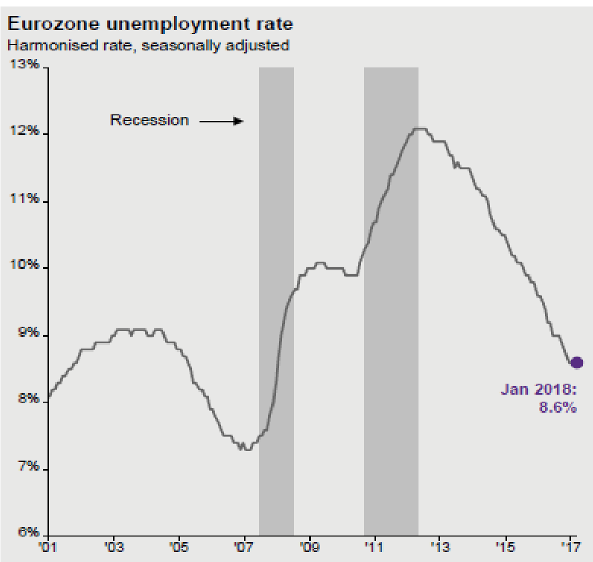
This second set of charts shows the low headline unemployment around the world.

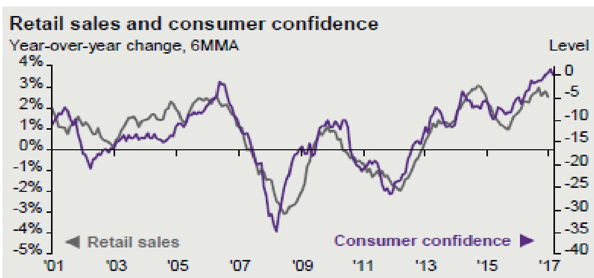
While wage growth is still modest – this could change, particularly in the USA.
However, all countries have significant proportion of the work force in part time, under employed situations – so there is still quite a lot of spare capacity left before the wage increases start to take place. The USA is the most likely country that this may occur in.

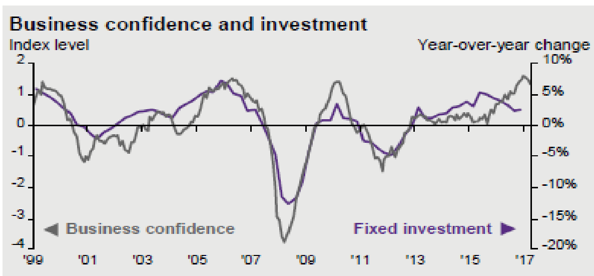


Even the Eurozone is picking up with good growth and consumer confidence.

Unemployment is down to almost 2006 levels – business confidence, consumer confidence and retail sales are up.







However, there are some nagging negatives foating about in both the global and Australian economy.

- Australian household debt is too high, at a time when property prices are slipping.
  Consumers have a habit of closing their wallets when property prices fall; a key link to the “wealth effect”.

  Consumer sentiment is weak and retail sales reflect that, just as major capital home prices are tipped to slip further.

- Global world trade has had static growth for nearly 10 years, with recent pronouncements suggesting more tariffs and less growth, if not shrinkage in trade.
- US government deficit forecast to grow significantly, with longer term impacts anticipated in a few years.
  If the US economy slows – then that will be reflected globally.

Overall we still hold a positive view for investments over the next 24 months – with an expectation that beyond that time frame there will be a softening of investment returns. This will occur with increased incidents of market volatility where we experience bouts of market nervousness, such as the sudden drop in January before a slow crawl back up.