Economic News July 2015

As we welcome in the new financial year, we reflect back on another year of solid returns despite a range of recent uncertainty both in Australia and overseas.

The recent focus has been on Greece's inability to meet its debt repayments. Whilst there is still a chance of more last minute negotiations, the risk of a default by Greece on all its debt commitments is high, as is the potential for its departure from the euro zone. In addition to the 1.5 billion euro loan repayment that is now due, Greece has to make a further 3.5 billion euro payment to the European Central Bank on the 20th July. In the absence of an agreement being reached, uncertainty will continue and markets are likely to remain volatile.

The Chinese share market which at times is more like a casino, having surged over 150% in twelve months has now dropped around 30% from its recent highs (and we thought our market was volatile!). This is due to Chinese residents using borrowed money to fund their stock purchases. The China Securities Regulatory Commission has responded by amending some of the rules governing how residents are allowed to borrow.

In Australia much of the attention has been on interest rates. The Reserve Bank of Australia (RBA) has been less than confident about our economy and for this reason has kept official interest rates at a record low of 2%. The RBA may be tempted to cut rates again to stimulate the economy but will likely be hesitant to do so given the current talk of a property bubble in Melbourne and Sydney.

A lower Australian dollar has helped commodity prices somewhat but its value may need to drop further to have a real impact. The resources sector has been slowing and this has an impact on the overall rate of growth in the economy. Unemployment will pay a crucial role. Although rates of unemployment are stable, wages growth has been slow. Consumers with high levels of debt seem to be nervous about spending, even if they are happy about the apparent rise in value of their homes.

Having seen interest rates around the world fall, policy makers in the US have signalled a rise in US interest rates at some stage. Many analysts believe that the US economy has recovered sufficiently to remove the monetary measures put in place, especially given that the unemployment rate has dropped from a high of 10% in 2009 to the current 5.5%.

Aged Care

Our aged care system touches the lives of millions of Australians. Currently, more than one million people receive aged care services, with over half a million people receiving support at home.

With Australia's ageing population, our current aged care system needs to change to keep up with future demand.

From the 1st July 2015, a number of changes were introduced to improve access and choice for consumers in aged care. The new Commonwealth Home Support Programme (CHSP) is one of the changes being made to help older people stay independent and in their homes and local communities for longer. The CHSP will be used to help people regain independence and function after a setback like an illness or a fall. The focus is so individuals can remain at or return home, rather than entering residential aged care. However, unlike transition care, new short-term restorative care will be available to people before they end up in hospital.

Some of our clients have had to consider aged care facilities for a family member. This can be a complex area that is full of unhelpful acronyms like RADs and DAPs.

If it will help, we can assist to identify solutions to important questions like:

- how can we reduce the accommodation payment?
- are the costs requested by the facility negotiable?
- how can we reduce the means tested fee?
- what impact will this have on any Centrelink or DVA benefits?

Age Pension changes

Last month, the Greens backed the Coalition Government's $2.4 billion pension reforms in a surprise deal. The outcome means the budget measure has now passed the Senate and is set to be introduced from 1st January 2017.

The reforms increase the lower level thresholds (to provide more Australians with the maximum age pension payment) and decrease the upper level thresholds for means testing (resulting in numerous Australians either having their entitlement to the age pension reduced or losing it entirely).

We have summarised the changes in the following table:

	Current threshold for full pension	Threshold from 1 January 2017
Homeowner:		
• Single	$202,000	$250,000
• Couple	$286,500	$375,000
Non-homeowner:		
• Single	$348,500	$450,000
• Couple	$433,000	$575,000

	Current threshold for part pension	Threshold from 1 January 2017
Homeowner:		
• Single	$775,500	$547,000
• Couple	$1,151,000	$823,000
Non-homeowner:		
• Single	$922,000	$747,000
• Couple	$1,298,000	$1,023,000

A person who loses eligibility to a pension on 1 January 2017 because of these changes will automatically become entitled to the Health Care Card or the Commonwealth Seniors Health Card (CSHC) if they are of pension age. Similarly, war veterans who lose eligibility to the service pension because of these changes will be entitled to retain their Veterans Gold Card.

Please note, from 20th June 2015, CSHC holders will no longer be paid the seniors supplement. The clean energy supplement will continue to be received.

Investment environment remains unpredictable

Improvements particularly in the US and UK economies provide a stable platform. However, issues such as Greece and China’s slowing economy remain unresolved. Whilst interest rates have fallen around the world, property and share markets have risen tremendously as investors look to obtain a better return than cash investments.

There is concern that investment valuations rest on the foundations of low interest rates. Slower growth in China, as it transitions to a more sustainable, consumer oriented economy has important consequences for Australia, especially in commodity prices. This is occurring at a time when the valuations of many traditional asset classes and securities are high and return potential is lower.

How are portfolios positioned?

We remain focused on insulating investment funds against adverse events using a conservative first approach. Portfolios have been structured to provide resilience in a wide range of economic scenarios such as increasing unemployment and lower interest rates. Portfolios are then adjusted to manage possible risks and take advantage of potential return opportunities. This approach means portfolios are well diversified.

As the market environment evolved this year, we made changes to portfolios to increase their defensive positioning. Portfolios have become cautiously positioned because our assessment is that the reward for taking risk is compressed. This is the kind of environment when managing risk is at least as important as generating returns.

Overall having had solid returns in recent years, we expect a return to more traditional long term averages albeit with volatility along the way as we encounter more challenging economic conditions in Australia and overseas.

As always, if you have any questions or wish to discuss anything please call us on 03 9544 1004.

Wishing you a very happy new financial year,

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