neo news
Financial Solutions
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What really influences interest rates?

Interest rates are very important for many Australians, and rightly so – after all, whether it's the returns on savings accounts or mortgage repayments, the rate of the day can have a significant impact on the household budget for millions of Australians. So what influences interest rates, and why are the changed?

Who's navigating?

One of the many responsibilities and functions of the Reserve Bank of Australia (RBA) is to control domestic official interest rates in order to fulfil their charter, contained in the Reserve Bank Act 1959, which is to best contribute to the:

- stability of the currency of Australia
- maintenance of full employment in Australia
- economic prosperity and welfare of the people of Australia.

As a result of this charter, the RBA has determined that an inflation rate of between two and three per cent per annum is the best way to meet these objectives.

Why do they change?

The RBA lowers official interest rates to make borrowing cheaper, increasing spending (and therefore demand), which in turn increases inflation to the desired range. Increasing rates, on the other hand, discourages borrowing – and spending – easing inflationary pressures.

While fulfilling their charter may be the goal of the RBA, the same may not be said for central banks around the world. Low interest rates are usually associated with a lower dollar as they often mean less foreign investment as global investors look elsewhere for the highest returns for their money. In what sometimes looks like a race to the bottom between nations, a lower dollar makes manufactured goods cheaper for foreign buyers, boosting exports and increasing tourism.

Why is my loan interest higher than the cash rate?

The RBA's cash rate provides a level of interest rates that affects the rates paid in the wholesale market by the banks.

While credit is available to banks in the wholesale market at a rate of, say the current 1.5 per cent, they will add a premium before applying the rate to retail loans and mortgages. The concept is the same as a supermarket buying produce in bulk at a lower price than offered to shoppers. Simply, this margin is how banks make their money.

In this issue...

Winners and losers from lower interest rates

Winners	Losers
Borrowers: mortgage holders and property investors benefit from lower repayments on loans.	**First home buyers**: lower interest rates contribute to the rise in house prices, meaning buying a first home just got harder.
Investors in overseas markets: international earnings benefit from a lower Aussie dollar.	**Insurance companies**: as insurance companies invest your premiums long-term, they are now facing lower returns which can put pressure on premiums.
Investors in the share market: due to low returns on fixed-interest investments, investors put more money into the share market.	**Savers**: reducing interest rates means lower returns on savings, affecting those who rely on interest for their income.

For the best investment strategy in the current low interest rate environment, talk to us today.

2017 Assets Test Changes

On 1 January 2017, important changes are happening to age pension payments. Whether you're currently enjoying retirement or just planning for it, it's important to understand these changes and be prepared early.

What are the changes?

There are two main ways your age pension payments may change.

Assets threshold changes

The first is the increase in the assets you may hold and still qualify for the full age pension. These changes are laid out in the table below:

	Assets test thresholds (as at 1 July 2016)	Assets test thresholds (from 1 January 2017)
Homeowner – single	$209,000	$250,000
Homeowner – couple	$296,500	$375,000
Non-homeowner – single	$360,500	$450,000
Non-homeowner – couple	$448,000	$575,000

However, while this may be good news, these changes also come with an increase in the taper rate.

Taper rate changes

Unfortunately, the increase in the taper rate means that when you reach your assets threshold, you will lose your full age pension faster. At the existing taper rate, you lose $1.50 in your pension for every $1,000 in assets you hold above these current limits.

From 1 January 2017 you will lose $3.00 in your pension for every $1,000 you have above the new limits.

Case study 1:

Bob, 67, is a widower who has paid off his house and has a nest-egg of $275,000 from a lifetime of working and his wife's life insurance. Currently he receives $774.90 per fortnight, however this will increase to $798.00 per fortnight from 1 January 2017.

Winners and losers

Generally speaking, the changes are a win for those with assets up to and around the new assets test threshold. However, those with higher assets will see the pension diminish faster, and cut out completely at lower levels.

	Part-pension cut offs (as at 1 July 2016)	Part-pension cut-offs (from 1 January 2017)
Homeowner – single	$791,750	$547,000
Homeowner – couple	$1,175,000	$823,000

At its most drastic level, married homeowners with savings in excess of $823,000 stand to lose $13,719 per annum. They would have to drawdown on their capital at a rate of 1.6 per cent, per year ($13,719/$823,000) to make up for the loss of the part age pension.

Case study 2:

Susan and Bruce are in their early 70's. They are home owners and have investments in the stock market worth $750,000 to support their retirement. Currently they receive $637.16 per fortnight in the part-pension, however this will fall to $192.40 per fortnight.

Remember!

Changes to the asset test should be considered in conjunction with the Income Test as **both** tests are applied to Centrelink benefits and the **worst** outcome is applied!

How might you be affected?

Grandfathered account based pensions?

Some of you may have locked in grandfathered account based pensions prior to 1 January 2015. If so, any cancellation of the age pension entitlements will forego the grandfathered status of the account based pensions.

Talking points: the impact of rising deeming rates over time will have on your financial situation.

Pensioner bonus scheme (PBS)

From 1 January 2017, changes to the asset test means some people, by virtue of their assets, will receive a lower age pension entitlement or be cut-off from the pension altogether, translating to a reduced PBS, or no PBS.

Talking points: apply for the PBS, if eligible, sooner rather than later if your level of assets preclude you from the pension.

Reduction of assets

Following the changes, for every $1,000 reduction in assessable assets, you may receive an additional $3.00 per fortnight of pension (currently $1.50 per fortnight of pension).

Talking points: any strategies or steps to reduce assets should be considered earlier rather than later.

Commonwealth seniors health card (CSHC)

If you lose your pension entitlement on 1 January 2017 as a result of the changes, you will be automatically issued with a CSHC, or a Health Care Card for those under age pension age. You will be exempt from the usual income test requirements for these cards indefinitely.

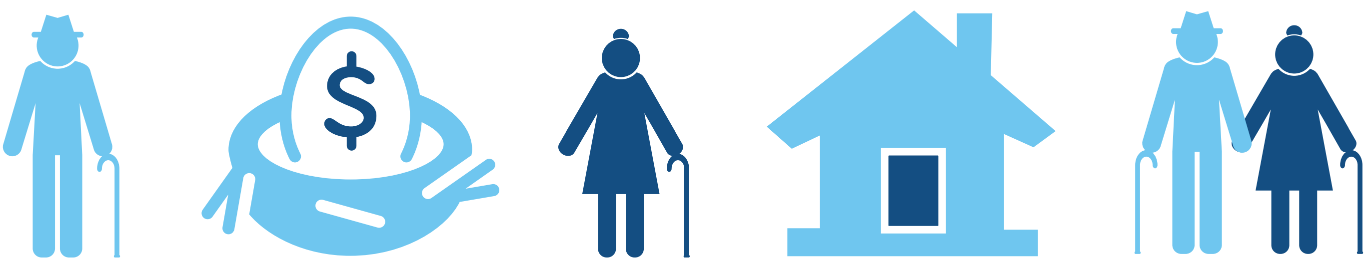
Talking points: you may qualify under the CSHC income test, if you're yet to receive income support.

Residential aged care members

For residents in residential/home care, receiving a lower or no age pension could translate to lower care fees. However, receiving less or no pension will put pressure on cashflow.

Talking points: renting out the home instead of selling it may be preferable as concessional Centrelink and aged care treatments apply.

To understand the impact on your specific circumstances and how best to prepare for these changes, please give us a call.



The election's over!
What can we expect now?

It's nearly two months since the Coalition was returned to Government. As Malcolm Turnbull and his team settle back into Parliament, one of the first items on the agenda will be passing of the May 2016 Federal Budget and in particular, superannuation reforms. However with an unexpectedly small margin of victory, this may not be as easy as they hoped.

We revisit the Government's main proposed superannuation amendments and the likelihood of them becoming law:

1. $500,000 lifetime cap on non-concessional contributions

Non-concessional contributions are those which are made from your after-tax salary. The Government has proposed a $500,000 lifetime cap on these contributions made from Budget night (3 May 2016) however will retrospectively include non-concessional contributions made since 2007. If you've already contributed more than $500,000 during this time, the extra amount will not be taxed but you won't be able to make any future contributions.

While the cap limit should get the support it needs to pass, the retrospective nature of the changes may be harder to get through Parliament.

2. Reduced concessional contributions cap and carry forward of unused cap amounts

Concessional contributions are before-tax contributions, which are taxed at up to 15 per cent for most people. The Government has proposed reducing the annual concessional contributions cap to $25,000 for everyone from 1 July 2017. However unused concessional cap amounts may be carried forward on a rolling basis over a consecutive five-year period.

While the carry forward provisions are popular, the reduction to the current cap ($30,000 for people under age 50 and $35,000 over age 50) and the effect this has particularly on older workers is unpopular, both inside the Government and outside.

3. Changes to transition to retirement strategies

The Government has proposed removing the tax exemption on earnings in a transition to retirement (TTR) pension - and therefore reducing the tax-effectiveness of a TTR strategy.

The Government is likely to get the support it needs from the ALP to get this through Parliament.

4. $1.6 million cap on pension assets

The Coalition proposal is for a cap on superannuation assets in the tax-free pension phase of $1.6 million from 1 July 2017, with the balance held in the taxable accumulation phase.

This should get through Parliament as the Government's recommendation is similar to that of the ALP.

The Government continues to make changes to the superannuation system to ensure it is fair and sustainable for all Australians in the years and decades to come. To help understand the changes and what opportunities there are for you, please don't hesitate to contact us.

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