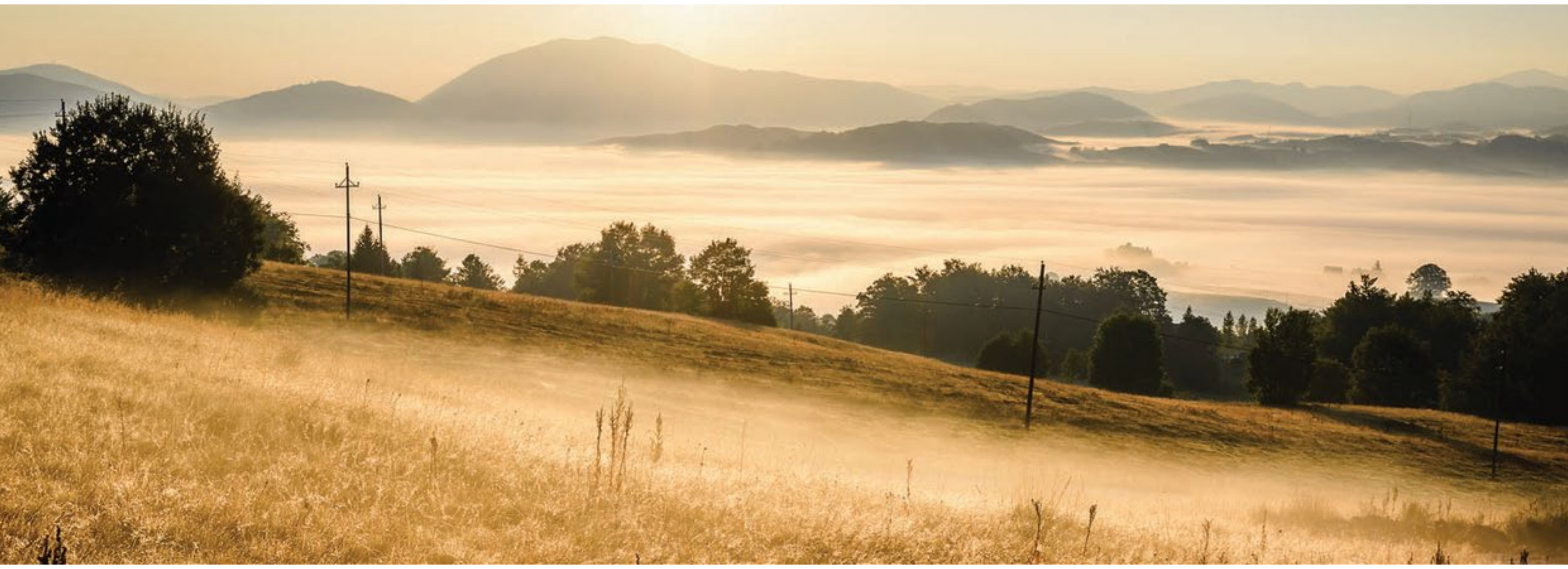

May 2022 Newsletter

Welcome to our May newsletter, and while the weather is cooling the economic and political landscape is heating up as the federal election campaign shifts into top gear ahead of the May 21 polling day.

The economic event that overshadowed all others in April was the release of the March quarter Consumer Price Index (CPI), which showed inflation up 2.1% in the quarter and 5.1% on an annual basis. This was the biggest lift in prices since 2001 and well above the Reserve Bank's target of 2-3%. The biggest increases were for fuel, housing construction, and food as the war in Ukraine pushes up global oil prices and the cost of transporting food and other goods. The Reserve Bank lifted official interest rates today from their current historic low of 0.1% to 0.35%; for many property investors this being the first rate rise that they have ever encountered. Rate rises will inevitably be passed through to variable mortgage rates, putting more pressure on household budgets during an election campaign where cost of living is a major theme. However, interest rate rises are not detrimental to everyone, particularly those without mortgage debt and self funded retirees who have desperately been seeking secure interest bearing returns.

On a positive note, unemployment fell below 4% in March, its lowest since 1974 as the economy continues to recover from COVID-related disruptions. As a result, businesses are more confident, with the NAB business confidence index lifting to a five-month high of 15.8 points in March, well above its long-term average of 5.4 points. Consumers are less confident, with the Westpac-Melbourne Institute consumer sentiment rating down 0.9% in April to a 19-month low of 95.8 points.

The Aussie dollar fell from US75c to around US71c over the month, adding to cost pressures on imported goods. Oil prices eased slightly, with Brent crude down 6% in April but up 48% on the year.

Experien Financial Services
P 1300 417 020
E superannuation@experien.com.au
W www.experien.com.au
Linkedin /company/experien-financial-services

THE ROAD AHEAD FOR SHARES

Trying to time investment markets is difficult if not impossible at the best of times, let alone now. The war in Ukraine, rising inflation and interest rates and an upcoming federal election have all added to market uncertainty and volatility.

At times like these investors may be tempted to retreat to the "safety" of cash, but that can be costly. Not only is it difficult to time your exit, but you are also likely to miss out on any upswing that follows a dip.

Take Australian shares. Despite COVID and the recent wall of worries on global markets, Aussie shares soared 64 per cent in the two years from the pandemic low in March 2020 to the end of March 2022.[i] Who would have thought?

So what lies ahead for shares? The recent Federal Budget contained some clues.

The economic outlook

The Budget doesn't only outline the government's spending priorities, it provides a snapshot of where Treasury thinks the Australian economy is headed. While forecasts can be wide of the mark, they do influence market behaviour.

Australia's economic growth is expected to peak at 4.25 per cent this financial year, underpinned by strong company profits, employment growth and surging commodity prices. Our economy is growing at a faster rate than the global average of 3.75 per cent, and ahead of the US and Europe, which helps explain why Australian shares have performed so strongly.[ii]

However, growth is expected to taper off to 2.5 per cent by 2023-24, as key commodity prices fall from their current giddy heights by the end of September this year.

Commodity prices have jumped on the back of supply chain disruptions during the pandemic and the war in Ukraine. While much depends on the situation in Ukraine, Treasury estimates that prices for iron ore, oil and coal will all drop sharply later this year.

Share market winners and losers

Rising commodity prices have been a boon for Australia's resources sector and demand should continue while interest rates remain low and global economies recover from their pandemic lows.

Government spending commitments in the recent Budget will also put extra cash in the pockets of households and the market sectors that depend on them. This is good news for companies in the retail sector, from supermarkets to specialty stores selling discretionary items.

Elsewhere, building supplies, construction and property development companies should benefit from the pipeline of big infrastructure projects combined with support for first home buyers and a strong property market.

Increased Budget spending on defence, and a major investment to improve regional telecommunications, should also flow through to listed companies that supply those sectors as well as the big telcos and internet providers.

But there are other influences on the horizon for investors to be aware of.

Rising inflation and interest rates

With inflation on the rise in Australia and the rest of the world, central banks are beginning to lift interest rates from their historic lows. Australia's Reserve Bank is now expected to start raising rates this year.[iii]

Global bond markets are already anticipating higher rates, with yields on Australian and US 10-year government bonds jumping to 2.98 per cent and 2.67 per cent respectively.[iv]

Rising inflation and interest rates can slow economic growth and put a dampener on shares. At the same time, higher interest rates are a cause for celebration for retirees and anyone who depends on income from fixed interest securities and bank deposits. But it's not that black and white.

While rising interest rates and volatile markets generally constrain returns from shares, some sectors still tend to outperform the market. This includes the banks, because they can charge borrowers more, suppliers and retailers of staples such as food and drink, and healthcare among others.

Putting it all together

In uncertain times when markets are volatile, it's natural for investors to be a little nervous. But history shows there are investment winners and losers at every point in the economic cycle. At times like these, the best strategy is to have a well-diversified portfolio with a focus on quality.

For share investors, this means quality businesses with stable demand for their goods or services and those able to pass on increased costs to customers.

If you would like to discuss your overall investment strategy don't hesitate to get in touch.

i https://www.commsec.com.au/market-news/the-markets/2022/mar-22-budget-sharemarket-winners-and-losers.html

ii https://budget.gov.au/2022-23/content/bp1/download/bp1_bs-2.pdf

iii https://www.finder.com.au/rba-survey-4-apr

iv https://tradingeconomics.com/united-states/government-bond-yield

Family trusts are a popular and effective investment structure to manage and protect your family's fortune, but you don't have to be worth a fortune to benefit from having one.

Despite their appeal, they are not for everyone. Indeed, it is suggested that if your assets are less than $300,000, and that is not counting your super, then it may well not be worth your while.

But for those with sufficient assets, a family trust can be an effective way to protect your family's assets and limit your tax liability at the same time. So how do they work?

What is a family trust?

A family trust is a discretionary trust, where assets are placed in the care of a third party, the trustee, who manages it on behalf of the beneficiaries.

Discretionary trusts are so named because the distribution each year of the income and capital gains earned by the trust to the beneficiaries is at the total discretion of the trustee.

Beneficiaries are members of the trust and might include parents, children, other close relatives, and their spouses. A beneficiary may also be a company.

Key benefits

As mentioned, the key benefits of a family trust are asset protection and tax minimisation. A trust provides protection from creditors in bankruptcy, but the contents of a trust can be included as part of the matrimonial pool when it comes to divorce.

All income of the trust, including realised capital gains, must be distributed each year. It is then included in the beneficiary's assessable income and taxed at their personal tax rate.

As a result, a trust can work particularly well from a tax viewpoint, if you are on a high marginal tax rate but your beneficiaries are on low marginal rates. If all individual beneficiaries are on a marginal tax rate greater than the company tax rate, then a family trust may include a corporate beneficiary to reduce tax.

More flexibility

Another advantage of a family trust is that it offers a flexible, tax effective structure to accumulate wealth for retirement alongside superannuation.

Their flexibility also makes them particularly attractive for small business owners who may run the business through a company structure but hold shares in that company in a family trust. The trust can then direct different types of income such as rental income from your business premises, franked dividends from company profits or capital gains to different individuals.

A family trust can also help with succession, allowing you to pass control of the family trust to the next generation by changing the trustee, without triggering a tax event.

There are some disadvantages too. There is the loss of ownership as the trust now owns the asset, not you. Also, if the trust suffers an investment loss, those losses cannot be distributed to offset your personal tax liability but must remain inside the trust. And there are costs involved in setting up and managing the trust.

Setting up a trust

To set up a family trust you will need to consult a lawyer to create a trust deed. You will also need to do the following:

- Appoint a trustee and determine your beneficiaries
- Decide which assets to include in the trust (a wide range of assets including stocks, bonds, managed funds, cash, real estate, antiques and fine art can all be included)
- Apply for an ABN and a Tax file number (TFN) and open a bank account in the name of the trust.

It can cost some $2500 to set up the trust and there will be annual fees as you have to file with the Australian Tax Office each year. Stamp duty applies in both NSW and Victoria on establishment but not in other states.

What about testamentary trusts?

Another type of trust popular with families is a testamentary trust which is created within your Will and does not come into effect until your death. Similar to family trusts, they have the advantage in estate planning of providing tax and asset protection benefits for the future.

Family trusts are popular for good reason, but you need to make sure it is appropriate for your family's circumstances. If you would like to know more, give us a call.