Welcome to the July 2018 Edition of the Martin Bros Monitor.

In this edition of the Martin Bros Monitor:

- The Trump Train Continues
- Budget Changes - 2018/19 FY

The Trump Train Continues

Despite the continual comedy show on how to handle international negotiations, Trump in his own style is achieving economic success on home soil. Some may argue that the ground work for this was done by the previous administration. It is true, he did inherit an economy well on the way to recovery. However, it's advancement since his election win is real. Initially global markets were shocked that the US sharemarket could advance after this so called "loose cannon" made it into the White House.

What global observers from the outside missed, seems to be the overwhelming support for his fiscal stimulus package. Small business confidence in the US is at an all time high. His pro America rhetoric backed up by fiscal changes has promoted jobs creation and capital investment domestically.

All of this has led to a US economy growing above trend (trend being circa 2.4% per annum GDP). Unemployment fell below 4% recently which is considered to be full employment (those that want a job have one). In the latest jobs data the unemployment rate jumped from 3.9% to 4.1%. Below this headline, which on the surface looks like a reversal in trend of the last 7 or so years, the news is actually positive. This increase in unemployment was brought about purely by a big jump in the participation rate. Some 500,000 additional people entered the jobs market. This usually occurs when confidence is up, as people believe it is worthwhile looking for work based on their likely success and the reward (pay) they can command. So US consumer confidence is high.

Perhaps Australia could learn a thing or two from the US experience. Hopefully not in the type of character we want to run our country, but in the fiscal stimulus and reform that has been brought about under the Trump administration. Remember, as we wrote last year in MBM, there were many smart people in the US working on the fiscal stimulus and change that Trump was spruiking about. His often crazy rhetoric is sometimes just that.

Australia's economy has been chugging along for many years now. Despite official interest rates still at Emergency levels, we have failed to boost GDP with any significance. This leaves us vulnerable to global shocks as it leaves the RBA little room to cut rates if needed due to external shocks. So why have we lagged behind the US? One obvious answer is the lack of political leadership and structural and / or fiscal reform. Our economic fall back seems to be infrastructure, infrastructure and infrastructure, both from a State and Federal level.

We're not suggesting that this infrastructure is not needed. In many cases it is overdue. However, infrastructure alone will not drive sustainable growth and break us out of the 2 and a bit % GDP band we've been stuck in for a very long time. Infrastructure investment has been necessary to counter the dramatic fall in resource investment that occurred post the GFC. It has and will continue to employ thousands of people and support firms involved in the infrastructure cycle (engineers, builders, contractors etc). But this is only a small part of our overall economic workforce.

Despite all of the infrastructure talk and action, the average small business and worker do not feel better off, or more confident in their future. Surely this has something to do with very little serious fiscal, structural and tax reform over the past two decades. Apart from the real benefits these types of reforms provide, a main factor in boosting GDP is CONFIDENCE. When people feel more confident they will spend more (retail) and invest more (small businesses are run by ordinary people who make decisions to invest in capital expansion or not based on how confident they feel). Business drives capital investment in people (jobs) and equipment (other business suppliers). The constant tinkering with regulations, superannuation laws, franking credits, etc does nothing but dent confidence.

Enough economic preaching from us!

In our Xmas edition of MBM last year we wrote:

"The global economy is definitely in a sweet spot with Europe, China and the US all performing well with solid (or improving) growth and employment. This should bode well for markets again in 2018, providing we see a return to more normal volatility (i.e. we see some sell offs of circa 10%). The more prolonged this ultra low volatility continues then the bigger the shock will seem when it comes – which there always is one – throughout market cycles."

The good news is we have seen volatility return to equity markets. Although this means that there will be quarters where we see lower portfolio values, this volatility is healthy for markets and also provides opportunities for further or re-balancing of investments.

As always, there are potential geo-political threats to global markets and the prospect of a sharp reversal in bond rates should inflation spike, but from an earnings perspective, which ultimately drives equity markets, the outlook is positive. Australia is low growth, Europe is improving and the US is expanding corporate earnings at a decent clip. There is no impending earnings hole on the horizon, which should be supportive of equity valuations for the rest of 2018 and into 2019.

Budget Changes - 2018/19

Since the last edition of the Martin Bros Monitor, the Federal Government has handed down the 2018/19 Budget. We detail below the main points of interest from an financial planning perspective:

Personal Income Tax Plan - legislated

- From 1 July 2018 the 32.5% top threshold will increase to $90,000 - see below for personal tax rates for the 2018/19 FY
- From 2018-19FY through to 2021-22FY a new tax offset of $530 will be available for low and middle income earners in addition to the Low Income Tax Offset (LITO) of $445
- From 2022-23 the 19% top threshold will increase from $37,000 to $41,000; and the LITO of $445 will increase to $645
- From 2022-23 the 32.5% top threshold will increase to $120,000
- From 1 July 2024 the 37% tax bracket will be abolished completely, reducing the number of tax brackets from five to four; and the top marginal tax rate of 45% will apply to incomes above $200,000
- The above changes will ensure Australians earning more than $41,000 will only pay 32.5% up to the top marginal tax rate; and will address tax bracket creep for the future

Income Range	Tax Rates
Up to $18,200	0%
$18,201 - $37,000	$0 + 19% over $18,200
$37,001 - $90,000	$3,572 + 32.5% over $37,000
$90,001 - $180,000	$20,797 + 37% over $90,000
$180,001	$54,097 + 45% over $180,000

"Protecting Your Super Package" - not yet legislated

Commencing 1 July 2019 the ATO will be given capacity to actively reunite Australians with their lost and inactive superannuation. This will help minimise account balance erosion via fees for those with multiple super accounts. Inactive accounts below $6,000 will be transferred to the ATO to protect from further erosion, and data matching will be used to connect with the member’s active accounts.

Fees will be capped on super accounts with balances less than $6,000 at 3%. Superannuation fund exit fees will be banned if the member is changing super providers.

Life insurance cover in superannuation for young savers under age 25 will be changed to an "opt-in" basis. Currently it is via an "opt-out" basis. Holding fewer automatic insurance policies will allow Australians to grow their balances faster and protect low balances from being eroded entirely. Opt-in will also be available for those with low balances or inactive accounts.

One Year Work Test Exemption - legislated

Australians aged 65 to 74 will be given a 12 month exemption from the superannuation work test to help boost retirement savings. The 12 months commences from the end of the financial year in which they last met the work test.

This exemption will apply where an individual’s total superannuation balance is below $300,000. This will allow voluntary superannuation contributions to be made in the first year following retirement. Existing concessional and non-concessional contribution caps will apply

Super Guarantee Contributions for High Income Earners - legislated

From 1 July 2018 some high income earners (above $263,157) with multiple employers will be able to nominate that their wages are not subject to Superannuation Guarantee. This will reduce the number of people who breach the $25,000 cap on concessional contributions, and allow some people to negotiate a higher income instead.

Other Changes

- Maximum amount of members in a Self-Managed Super Fund (SMSF) raised to 6 from 4.
- Centrelink Pension Loan scheme to allow Age Pensioners to unlock equity in their home expanded (income now up to 150% of age pension entitlement)
- Pension Work Bonus increased to allow Age Pensioners to earn up to $300 per fortnight without effecting their Centrelink payment (up from $250 per fortnight)

We also note changes from early budgets which are now in force from 1 July 2018:

- Individuals aged 65 and over will be able to make a non-concessional contribution of up to $300,000 in proceeds from the sale of a principal residence, held for at least 10 years, into their superannuation without meeting the work-test. These new contributions will be in addition to any other voluntary contributions that people are able to make under the existing contribution rules and concessional and non-concessional caps.
- Catch up' concessional contributions into super by allowing unused concessional contribution caps to be carried forward on a rolling basis for up to 5 consecutive years where an individual's account balance is $500,000 or less. This will provide flexibility to those individuals who experience interrupted work patterns or have irregular capacity to make contributions to help boost superannuation savings. Only unused amounts accrued from 1 July 2017 can be carried forward.

Should you have any queries with regards to any of the above mentioned changes, please do not hesitate to contact us.

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