

Global Markets navigate a sea of uncertainty

It's almost a decade since the global financial crisis created havoc in financial markets. While the global economy continues to show signs of recovery, political uncertainty in Europe and the United States is creating fresh confusion on global markets as investors wait to see how current events play out.

It started just over a year ago when Britain voted to leave the European Union. 'Brexit' as it became known was followed by the surprise election of President Trump in the United States. Then the relatively unknown and politically unaligned Emmanuel Macron won the French Presidential election. And most recently, UK Prime Minister Theresa May gambled on a general election to strengthen her hand going into the Brexit negotiations with the EU, only to end up with a hung parliament.

That's a lot of unpredictable outcomes for one year. As every investor knows, markets don't respond well to uncertainty. So what can we expect in the months ahead?

Brexit talks begin

Brexit negotiations are finally underway but Britain's lack of political unity may prolong talks and weaken its hand. The process involves two stages – first there are the technical negotiations over who gets what in the divorce. This will be followed by crucial trade talks about the nature of Britain's relationship with the EU and its 27 member states going forward.

As at April 2017, 47 per cent of the UK's total exports and 51 per cent of imports were to and from the EU.¹ UK business leaders are calling for a 'soft' Brexit which would allow for the continuation of tariff-free trade in goods and services between Britain and the EU's 27 members. But some conservatives are pushing for Britain to go it alone, or a 'hard' Brexit.

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Whichever way the talks go, there are likely to be financial winners and losers. The early market response has been to sell down the value of the British pound and British shares, although a weaker pound is good news for companies with foreign earnings.

The market has responded more positively to President Macron's victory and the success of his new party's candidates in France's June elections. Macron has promised market-friendly reforms to boost the sluggish French economy.

As the Trump trade deflates

The market's early positive response to the election of President Trump has lost momentum as key policy changes including tax cuts and infrastructure spending which were intended to boost economic growth now look in doubt.

With the focus on political uncertainty on both sides of the Atlantic, the US Federal Reserve's latest rate rise barely registered on financial markets. The Fed raised its key interest rate for the third time in six months to a range of 1 per cent to 1.25 per cent, with one more rise anticipated this year. This signalled the central bank's ongoing confidence in the slow but steady economic recovery.

Markets appear to be playing a waiting game, with no clear signal to push the US dollar or bond yields higher. After a record-beating run, US shares have held onto their gains but drifted sideways in recent months. The S&P 500 index rose about 18 per cent in the year to June.ⁱⁱ

Australian and World Share Price Indices

Log Scale, End December 1994 = 100



Sources: Bloomberg; MSCI; RBA

Australia's growth continues

Closer to home, Australia's record-breaking economic run continues. While growth slowed to 1.7 per cent in the March quarter as the economy was hit by bad weather, low wages growth and slow consumer spending, it was a far cry from the recession some pundits were predicting.

The residential property boom in Sydney and Melbourne is also cooling.ⁱⁱⁱ In the three months to May, Sydney prices were steady while Melbourne prices rose just 0.7 per cent. Prices in Perth, Hobart, Darwin and Canberra fell while Adelaide and Brisbane posted catch-up gains. While this is good news for homebuyers, it also gives the Reserve Bank more room to lower interest rates to stimulate the economy if needed.

For the first half of the year, the Aussie dollar traded in a relatively narrow band around US75c. This was up from its low of US68c in January last year, but in recent weeks it has tested the US80c level. Longer term, the trend is likely to be down as the gap between local and US interest rates closes and foreign money looks for better returns elsewhere.

Australian shares have performed well, up more than 11 per cent in the year to June.^{iv} But to put this in perspective, along with the US market rise of 18 per cent, French, German and UK shares rose around 27 per cent, 34 per cent and 22 per cent respectively.^v In Asia, the Japanese market has been the standout performer with a rise of 29 per cent.

Looking ahead

Despite political challenges and uncertainty, global share markets continue to hit new highs while, as the graph shows, local shares are below their pre-GFC peak. For local investors, Australian shares remain attractive for their yields but global shares are likely to continue to provide superior returns going forward.

If you would like to discuss your investment strategy in the light of current world political and economic events, don't hesitate to give us a call.

i. https://www.uktradeinfo.com/Statistics/OverseasTradeStatistics/Pages/EU_and_Non-EU_Data.aspx

ii. All market figures as at June 27.

iii. <https://www.corelogic.com.au/news/multiple-indicators-point-to-softer-housing-market-conditions>

iv. <http://www.marketindex.com.au/asx200>

v. <https://tradingeconomics.com/stocks>



Technology To Get You Moving

If the ancient Greek Olympians could see the way the average Joe Athlete works out today... well, they might not even recognise it as exercise. Thanks to modern technology and the way the internet helps spread fads, the last few years have seen some truly weird and wonderful fitness trends emerge.



If you've recently spotted someone wearing what looks like two watches at once, chances are that at least one of their accessories was a wearable fitness tracker. Some of these gadgets look like watches, and others are disguised as simple bracelets with hidden buttons or one-way-mirror-style displays. Basic models track steps and time, whilst advanced models track everything from distance (using GPS) to heart rate zones tailored to your height, weight and age.

Challenge yourself with apps

Then there are the smart phone apps that take you beyond your normal running playlist. Take Strava for example.ⁱ If you like a bit of healthy competition, Strava lets you track and record your running and riding via GPS. Users are able to compare their performance over time and compete with other users for best times.

Other apps purposefully encourage walking a healthy distance. The 10,000 step challenge is a popular one, using GPS to track the number of steps you take per day, with the ultimate aim of walking the equivalent of eight kilometres.

Tech to help with healthy eating

On the other side of the wellness coin, medical professionals have worked with engineers to develop some fascinating tools for helping people to correct their eating habits. For example, the HAPIfork uses haptic feedback, and a smart phone app, to encourage fast eaters to cool their jets.ⁱⁱ

For those who struggle to cook whole foods from scratch, the humble food processor has had some welcome makeovers over the years. Today's

WiFi-enabled models connect to mobile apps and can cook or chill as well as process. They'll do just about everything for you save plating up and pouring you a nice drink to go with your meal.

A cost-effective way to stay healthy

The great thing about this new technology is that getting a hand with your health and wellbeing can be very cost effective. Some of the most popular phone and tablet apps can even be downloaded free of charge. But while apps may help keep you engaged and motivated, that's not to say you can (or should) get rid of your personal trainer or dietician. Rather, technology and 'fun' fitness classes are a great way to complement your existing routine.

Three popular gadgets and apps



Fitbit is perhaps the most well-known wearable fitness tracker on the market. Depending on the model you get, it can track everything from your steps and altitude travelled, to your heart rate and sleeping patterns. You can set goals, look for patterns in your stats, and even share your info with your trainer or doctor.



Couch to 5K is a smart phone app that's popular with those new to running or trying to get back into shape. It provides a staged approach to developing stamina and fitness, working up to running five kilometers.



Calorie Counter by MyFitnessPal is a nutrition and fitness app that's great for those who have trouble balancing calories in versus calories out. It integrates with a variety of fitness trackers, as well as being a standalone app.

What's next?

So what's next for the fitness industry in 2017? Well, if game fans have their way, you'll see more virtual reality fitness games. There's one out right now where you can sit on the stationary bike and suddenly you're not just cycling, you're riding the Tour de France in the Alps.

There is a lot of choice out there and it's really up to you to find the device or app that's going to keep you enthusiastic and challenged enough to meet your fitness goals. Even if you're just looking for some inspiration to get you off the couch - pick up your phone or grab a fitness tracker and get moving.

ⁱ <https://www.strava.com>

ⁱⁱ <https://www.hapi.com/product/hapifork>

Superannuation death benefits from 1 July 2017

Estate planning arrangements will be more complicated from 1 July 2017 for couples who have combined superannuation interests in excess of \$1.6 million.

Prior to 1 July 2017, the simple estate planning solution for these clients was to pay death benefits to the surviving spouse as one or more superannuation death benefit pensions. The introduction of the \$1.6m transfer balance cap upsets that simplicity, as the superannuation death benefit pensions will be assessed against the surviving spouse's transfer balance cap.

The alternative to paying a benefit as a pension is payment as a lump sum payment, which cannot be rolled over and must be taken out of the superannuation environment. The ongoing tax impact may be significant, depending on the level of taxable income of the surviving spouse.

A single individual over age 65 will generally not pay any tax if their taxable income is \$32,278 or less. But the effective marginal tax rate on taxable income in excess of this threshold is at least 31.5 per cent, and may be as high as 56.5 per cent.

In contrast, keeping the funds in the superannuation environment subject to tax at a maximum rate of 15 per cent is attractive.

An effective strategy for the surviving spouse is to commute his or her existing superannuation pensions back to the accumulation phase. Assuming the existing pensions are account-based pensions, a commutation will result in a transfer balance cap debit amount equal to the value of the pension commuted, effective from the date of the commutation.

The debit will reduce the balance in the surviving spouse's transfer balance cap, potentially creating capacity for the transfer balance cap credit associated with the reversion or commencement of a non-reversionary superannuation death benefit pension within the \$1.6 million cap.

Timing of the transfer balance cap debits and credits are important in terms of reducing the possible penalties associated with being in excess of the cap. If the transfer balance cap credit occurs before the debit, an excess position may result. Tax will be payable based on the notional earnings calculated on the excess amount at the ATO's general interest charge rate (8.73 per cent per annum in the July-September 2017 quarter). The tax rate applicable will be either 15 per cent or 30 per cent for subsequent breaches.

Reversionary pensions are attractive as the transfer balance cap credit does not occur until 12 months from the deceased's date of death. The transfer balance cap credit amount is the value of the pension at the date of death.



In contrast, a non-reversionary death benefit pension will result in a transfer balance cap credit effective when the pension is commenced, based on the value of the pension at commencement.

Typically, the reversionary pension transfer balance cap credit timing will allow more time for the surviving spouse to arrange commutation of any existing pensions, and potentially avoid possible transfer balance cap excess penalties that might otherwise arise. In addition, because the value of the transfer balance cap credit (ie the value of pension as at the date of death) is known before the credit occurs, the amount of commutation of any existing pensions can be precisely determined.

For these reasons, we expect that new account-based pensions will be more commonly established with a spouse as a reversionary beneficiary where the \$1.6 million transfer balance cap is likely to be an issue for the surviving spouse upon the death of the other spouse. In some cases, it may even be worthwhile to alter existing pension arrangements to allow reversionary nominations to be made.

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