INSIDE

AUGUST 2023

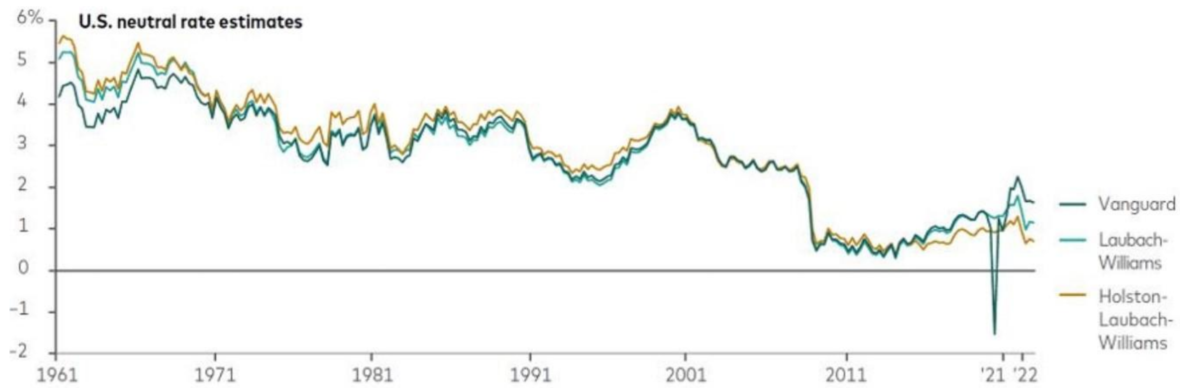
FINANCIAL MATTERS AFFECTING YOUR LIFESTYLE

Vanguard Economic & Market Update

Vanguard's latest forecasts for investment returns and our region-by-region economic outlook.

The neutral rate of interest in the United States may be higher than many people think—including Federal Reserve policymakers. That is among the findings of new Vanguard research that suggests current monetary policy may be less restrictive than generally assumed. Demographics began to push the neutral rate higher before the COVID-19 pandemic, the research finds, and fiscal deficits have accelerated the rise since.

The dividing line between tight and loose monetary policy may be higher than policymakers think



Notes: The Laubach-Williams and Holston-Laubach-Williams estimates of the U.S. neutral rate of interest are derived from Federal Reserve Bank of New York models. The Vanguard estimate is based on 2023 research by Joseph H. Davis, Ryan Zalla, Joana Rocha, and Josh Hirt.

Sources: *Vanguard and Federal Reserve Bank of New York model estimates of the neutral rate through 2022.*

The neutral rate is the theoretical central bank interest rate target that would neither restrict nor fuel activity in an economy at full employment. Assessments of the neutral rate, also known as R-star, are essential to policy-setting.

Vanguard's neutral-rate estimate is about half a percentage point higher than the estimate produced by the Laubach-Williams model, the Fed's most frequently cited neutral rate source, named for its economist authors. We ran our higher neutral-rate assessment through the Fed's macroeconomic model under a range of monetary policy rules. The results suggested that the median effective rate target would peak at 6% in 2023. The Fed's current rate target is 5%–5.25%.

In the longer term, the median central bank target rate would need to settle at 3.5%, or a full percentage point higher than the median long-run outlook in the Fed's most recent Summary of Economic Projections. These "higher for longer" findings support the idea put forth by Joe Davis, Vanguard's global chief economist, in his January *Wall Street Journal* commentary suggesting that long-term investors stand to benefit from a new era of "sound money."

The views below are those of the global economics and markets team of Vanguard ***Investment Strategy Group*** *as of July 19, 2023.*

Region-by-region outlook

Australia

A change at the top is unlikely to significantly alter the policy approach of the Reserve Bank of Australia (RBA). The government announced on July 14 that Michele Bullock would replace Philip Lowe as governor when Lowe's seven-year term expires on September 18.

We're watching developments related to interest-rate targeting as potentially more significant than the

leadership change. A recent recommendation of an external review of the RBA would clarify the bank's inflation target as the midpoint of the current 2%–3% range. "Assuming this recommendation is implemented in 2024, as widely expected, this adds a hawkish tilt to RBA policy so long as inflation remains above target," said Alexis Gray, a Vanguard senior economist.

While the RBA left its cash rate target unchanged at 4.1% on July 4, we expect above-target inflation to spur the central bank to raise its cash rate target to 4.6% and leave it there at least until 2024.

Headline inflation registered its smallest increase in 13 months in May, up 5.6% compared with a year earlier. Excluding food, automotive fuel, and holiday travel, prices were 6.4% higher in May. We expect headline inflation to fall to around 4.5% by year-end, as higher interest rates dampen demand, and to reach the RBA's 2%–3% target in late 2024 or 2025.

We continue to expect economic growth of 1%–1.5% for all of 2023, though risks skew to the downside. Our proprietary leading indicators model suggests that growth will fall below trend in the coming quarters amid weak consumer confidence and subdued consumption. We assign about a 40% probability of recession over the next 12 months.

United States

The most recent inflation and labour reports suggest some cooling in the economy ahead of a July 26 monetary policy announcement by the Federal Reserve.

The Consumer Price Index rose 3% on a year-over-year basis in June, down from 4% in May. Core prices, which exclude food and energy, were 4.8% higher, down from 5.3% the month before. However, the path to the Fed's 2% inflation target is likely to be long and winding. We expect year-over-year core inflation to finish 2023 around 3.3%, and that it will not fall below 2% until 2025.

Employers added 209,000 jobs in June, the fewest since December 2020, when there were net job losses.

But the unemployment rate fell to 3.6%, within the 3.4%–3.7% range that has prevailed since March 2022.

Wage growth remained strong—average hourly earnings were up 4.4% year-over-year in June—as the demand for workers continues to outstrip labour supply. We believe that gives Fed policymakers impetus to raise their target for short-term interest rates by 25 basis points (0.25 percentage point) on July 26.

At its last monetary policy meeting, on June 14, the Federal Open Market Committee voted to pause its interest rate hiking cycle, holding its rate target to a range of 5%–5.25%. In its "dot plot," an aggregation of Fed officials' individual views, the Fed suggested its rate target would be 5.5%–5.75% by year-end. That's 25 basis points above our 5.25%–5.5% forecast range.

China

Official data released on July 17 put an exclamation point on China's relatively weak economic performance. Gross domestic product (GDP) grew 6.3% in the second quarter compared with a year earlier, but that was a percentage point below analysts' consensus estimate. Although growth topped the first quarter's 4.5% pace, it owed in large part to favourable year-earlier comparisons. More telling: Compared with the first quarter, GDP grew just 0.8%.

We recently lowered our full-year growth forecast to a range of 5.5%–6%. Uncertainties around meaningful policy stimulus pose a downside risk not only to our forecast but also to the government

growth target of "around 5%." Developments at the Politburo meeting scheduled for the end of July will say a lot about the potential for further downside.
"We anticipate further stimulus measures to remain relatively modest," said Grant Feng, a Vanguard senior economist. "That could take the form of expanded policy bank financing for high-end manufacturing and the green sector, a modest policy rate cut of 10 to 20 basis points, and further relaxation of housing purchase restrictions."

Consumer prices fell for a third consecutive month in June and were flat compared with a year earlier. Producer prices, meanwhile, were down by a greater-than-expected 5% year-over-year in June. We foresee full-year headline inflation in a range of 1%–1.5% and core inflation, which excludes food and energy prices, of 1%.

Euro area

Weak recent data, especially from Germany, the euro area's largest economy, suggest that a recession continued between April and June, marking a third consecutive quarterly contraction.
"Weakness in the euro area has been broad-based across manufacturing and services," said Shaan Raithatha, a Vanguard senior economist. "That's consistent with another mild quarterly contraction in GDP, which would extend the recession."

We expect the peak impact of monetary policy tightening to take hold in the second half of 2023, with the labour market weakening in the European Central Bank's (ECB's) continuing quest to bring inflation to its 2% target. We continue to anticipate full-year economic growth of 0.5%, though risks are now skewed to the downside.

The pace of both headline and core inflation, which excludes energy, food, alcohol, and tobacco prices, stood at 5.5% on a year-over-year basis in June. We believe that still-too-high inflation will lead the ECB to raise its deposit facility rate by a further 25–50 basis points to a peak of 3.75%–4%, with no rate cuts until mid-2024.

United Kingdom

A day after government data showed an unexpected rise in core inflation, the Bank of England (BOE) on June 22 announced a 50-basis-point (0.5 percentage point) increase in the bank rate, to 5%. We recently raised our forecast for the BOE's peak rate by 75 basis points to a range of 5.5%–5.75%, given the stronger-than-expected inflation data, a continued tight labour market, and accelerating wage growth. We maintain our view that the BOE will not lower its rate target until mid-2024 at the earliest.

"The U.K. has had the worst of both worlds when it comes to inflation," said Shaan Raithatha, a Vanguard senior economist. "Its labour market has faced challenges like those in the United States, with lingering COVID-related supply issues, and its energy-price shock has been worse than in the euro area, given domestic price-setting mechanisms. That's why the Bank of England still has work to do to get inflation down toward target."

We expect year-over-year core inflation, which excludes food and energy prices, to end the year at around 4.9% and to average 5.3% in the fourth quarter, still well above the BOE's 2% target.

We foresee zero economic growth for the full year. Our base case is for recession in 2023, though the likelihood has increased that recession may be delayed into 2024. Resilience is partly attributable to changes in the U.K. mortgage market since the 2008 global financial crisis. Fewer households hold

mortgages today, and among those that do, more have rates that are fixed for 2 or 5 years rather than variable. As such, higher interest rates take longer to affect households.

Emerging markets

Emerging markets led the global rate-hiking cycle. As tighter monetary policy conditions cause economies to slow and help inflation recede toward central bank targets, we expect emerging markets to lead the rate-cutting cycle as well. That development could play out this month in Chile, where minutes of the June meeting of Banco Central Chile indicate the possibility of multiple rate cuts this year.

“Chile’s central bank is likely to be the first in Latin America to cut rates,” said Vytas Maciulis, a Vanguard economist. “Inflation, though still high, has fallen consistently, inflation expectations have dropped to the bank’s 3% target, and the broad economy has faltered.”

The Bank of Mexico left the target for its overnight interbank rate unchanged at 11.25% in June. The rate target remains more than 7 percentage points higher than where it stood when the bank’s hiking cycle began in June 2021. We believe the bank is likely to have reached its rate peak but don’t anticipate rate cuts in 2023.

We anticipate global emerging markets growth of 3.9% in 2023, but the recent economic developments in China, the world’s second-largest economy, bear watching. We foresee emerging Asia leading the way with 2023 growth of around 5.25%. We anticipate growth of about 1.5% in Latin America and of around 1% in central Europe, the Middle East, and Africa.

Canada

When the Bank of Canada (BOC) raised its overnight rate target to 5.0% on July 12, it cited a familiar theme: “The accumulation of evidence that excess demand and elevated core inflation are both proving more persistent.” Since the start of its hiking cycle in March 2022, the BOC has raised its overnight rate target by 4.75 percentage points.

We believe the BOC has reached its peak rate target, though risks skew to the upside. “Of particular note is the role of immigration within the labour and housing markets,” said Asawari Sathe, a Vanguard senior economist. “The immigrant share of the population is at its highest level in decades, and that’s keeping both labour supply and housing demand strong.”

The Canadian economy created 60,000 jobs in June, three times expectations and the most since January 2023. Even as the employment rate rose, so did the unemployment rate, to 5.4%, as more people sought work. We expect unemployment to edge up to about 5.5% by year-end as monetary policy slows the economy.

We expect inflation (+2.8% at the headline level, year-over-year, in June but +3.6% excluding food and energy) to continue to moderate this year. Upside risks remain, however, in part because shelter costs remain high in a home loan market dominated by variable-rate and short-term fixed-rate loans.

We continue to foresee 2023 economic growth of less than 1%, with risks to the downside, and a recession late in the year as the effects of higher interest rates spread.

Vanguard’s outlook for financial markets

Our forecasts are derived from a May 31, 2023, running of the Vanguard Capital Markets Model®. Figures are based on a 2-point range around the 50th percentile of the distribution of return outcomes for equities and a 1-point range around the 50th percentile for fixed income.

Following are our 10-year annualised return forecasts. Forecasts are from the perspective of investors in local currencies.
Australian stocks: 4.3% to 6.3%; **ex-Australia stocks:** 5.0% to 7.0%.
Australian bonds: 3.4% to 4.4%; **ex-Australia bonds:** 3.6% to 4.6% when hedged in Australian dollars.

About the Vanguard Capital Markets Model

IMPORTANT: The projections and other information generated by the Vanguard Capital Markets Model regarding the likelihood of various investment outcomes are hypothetical in nature, do not reflect actual investment results, and are not guarantees of future results. VCMM results will vary with each use and over time.

The VCMM projections are based on a statistical analysis of historical data. Future returns may behave differently from the historical patterns captured in the VCMM. More importantly, the VCMM may be underestimating extreme negative scenarios unobserved in the historical period on which the model estimation is based.

The Vanguard Capital Markets Model® is a proprietary financial simulation tool developed and maintained by Vanguard's Investment Strategy Group. The model forecasts distributions of future returns for a wide array of broad asset classes. Those asset classes include U.S. and international equity markets, several maturities of the U.S. Treasury and corporate fixed income markets, international fixed income markets, U.S. money markets, commodities, and certain alternative investment strategies. The theoretical and empirical foundation for the Vanguard Capital Markets Model is that the returns of various asset classes reflect the compensation investors require for bearing different types of systematic risk (beta). At the core of the model are estimates of the dynamic statistical relationship between risk factors and asset returns, obtained from statistical analysis based on available monthly financial and economic data. Using a system of estimated equations, the model then applies a Monte Carlo simulation method to project the estimated interrelationships among risk factors and asset classes as well as uncertainty and randomness over time. The model generates a large set of simulated outcomes for each asset class over several time horizons. Forecasts are obtained by computing measures of central tendency in these simulations. Results produced by the tool will vary with each use and over time.

The primary value of the VCMM is in its application to analysing potential client portfolios. VCMM asset-class forecasts—comprising distributions of expected returns, volatilities, and correlations—are key to the evaluation of potential downside risks, various risk–return trade-offs, and the diversification benefits of various asset classes. Although central tendencies are generated in any return distribution, Vanguard stresses that focusing on the full range of potential outcomes for the assets considered, such as the data presented in this paper, is the most effective way to use VCMM output.

The VCMM seeks to represent the uncertainty in the forecast by generating a wide range of potential outcomes. It is important to recognise that the VCMM does not impose "normality" on the return distributions, but rather is influenced by the so-called fat tails and skewness in the empirical distribution of modelled asset-class returns. Within the range of outcomes, individual experiences can be quite different, underscoring the varied nature of potential future paths. Indeed, this is a key reason why we approach asset-return outlooks in a distributional framework.

Indexes used in Vanguard Capital Markets Model simulations

The long-term returns of our hypothetical portfolios are based on data for the appropriate market indexes as of December 31, 2021; December 31, 2022; and May 31, 2023. We chose these benchmarks to provide the most complete history possible, and we apportioned the global allocations to align with Vanguard's guidance in constructing diversified portfolios. Asset classes and their representative forecast indexes are as follows:

Australian equities: MSCI Australia Index.

Global ex-Australia equities: MSCI All Country World ex-Australia Index.

Australian bonds: Bloomberg Australian Aggregate Bond Index.

Global ex-Australia bonds: Bloomberg Global Aggregate ex-AUS Bond Index.

This article contains certain 'forward looking' statements. Forward looking statements, opinions and estimates provided in this article are based on assumptions and contingencies which are subject to change without notice, as are statements about market and industry trends, which are based on interpretations of current market conditions. Forward-looking statements including projections, indications or guidance on future earnings or financial position and estimates are provided as a general guide only and should not be relied upon as an indication or guarantee of future performance. There can be no assurance that actual outcomes will not differ materially from these statements. To the full extent permitted by law, Vanguard Investments Australia Ltd (ABN 72 072 881 086 AFSL 227263) and its directors, officers, employees, advisers, agents and intermediaries disclaim any obligation or undertaking to release any updates or revisions to the information to reflect any change in expectations or assumptions.

Source:
https://www.vanguard.com.au/personal/learn/smart-investing/markets-and-economy/investment-and-economic-outlook-july-2023

Unlocking the Potential of Aged Pension and Superannuation Benefits

The Australian Aged Pension scheme provides a wonderful safety net for those with limited assets in retirement, although many remain confused by how their age pension entitlements differ from so called superannuation income streams.

The Federal Government provides an income for all Australians who reach pension paying age, currently set at age 67, who can prove they are an Australian resident and can also pass the income and asset tests or means test.

If you are part of a couple who own a home, you can qualify for a full age pension of $41,704 a year; if excluding your home, your other assets, including super, total less than $419,000 and can qualify for an ever-reducing part-pension, until your assets reach $954,000 a year.

The income test allows a couple to earn up to $8,763 a year from investments and still receive the full age pension, and up to $92,144 a year and receive a partial pension. In assessing your income, Services Australia applies a complex formula called **'deeming'**.

The deeming rules assume you earn at least 0.25 per cent a year on the first $93,600 in assets for a couple and then assume you are earning at least 2.25 per cent a year on your remaining assets. You must pass both tests to receive a pension and Services Australia will use the test that leads to the lowest entitlement.

In addition to the income from investment assets, you can also receive income from genuine employment of up to $7,800 a year under the Work Bonus scheme and still receive a full pension. This was temporarily increased to $11,800 a year between December 1, 2022 and December 31, 2023.

The rates and limits vary depending on whether you are a homeowner or not and whether you are part of a couple. Superannuation is included as part of the assets and income test, although superannuation can provide income support in addition to the aged pension.

So, superannuation sits alongside the age pension scheme, effectively topping up the pension or other income older Australians receive as they move into retirement. It is not subject to any limitations or qualifying factors.

Once you reach preservation age, which is 60 years of age for most people, you can effectively start your own private pension from your superannuation account. Once you do this, all the assets within super supporting this pension become tax-free in terms of earnings and capital gains. The income received is also tax-free in your hands.

This can significantly benefit older Australians as it means that they can effectively start a private pension to top up their age pension entitlements. For many, this makes the difference between living from one pension payday to the next, to having a bit of spare cash to help them get by.

The asset and income tests provide generous limits for older Australians to qualify for the age pension, with most of the so-called loopholes for effectively 'hiding assets' from Services Australia having been closed or significantly reduced.

Importantly, the family home is excluded from the asset test, meaning a potential age pension recipient can have millions of dollars tied up in their own home and still qualify for the full age pension, depending on the size of their remaining assets.

For couples with a significant age difference, it is also possible to effectively move assets from the older partner into the younger partner's superannuation account, where it won't be included in the asset test.

As long as the younger partner is under Age Pension age themselves, and their superannuation account is still in accumulation mode or can still receive contributions, the assets held within that account will not be included by Services Australia when assessing the couple's overall assets.

It is important to remember that when moving funds from one partner to another, you can contribute up to $110,000 in one financial year as a non-concessional contribution and $330,000 as a non-concessional contribution in any three financial year period under the "three-year bring forward" rule.

With some simple planning, it is possible to contribute up to $440,000 from one partner to a younger partner in a relatively short timeframe and so reduce the assets included in the age pension asset test accordingly.

These rules, though, are extremely complex and are best utilised under the guidance of a qualified financial planner to ensure you make the right decisions and avoid any costly mistakes.

Sources:

https://retirementessentials.com.au/age-pension/eligibility 'Retirement Essentials', Retirement Essentials, 2023 (Accessed 25 May 2023).

https://www.servicesaustralia.gov.au/who-can-get-age-pension 'Who can get it?', Services Australia, 2023 (Accessed 25 May 2023).

Why you may never retire

Millennials in Australia are facing an unprecedented challenge when it comes to planning for retirement. Many will never fully retire, as they will be unable to accumulate the necessary funds to support themselves for an extended period of time. With the cost of living steadily increasing, and many millennials grappling with large debts and limited financial resources, it is likely that more people will have to work well into their golden years.

How much is needed for a comfortable retirement?

According to the Association of Superannuation Funds of Australia (ASFA), an individual requires approximately $48,266 per year for a comfortable retirement. This amount increases to $68,014 per year for couples. However, the average superannuation balance for a 30 year old millennial is currently just $38,386, which is well below what is required for a comfortable retirement. As a result, many people in this age group are unlikely to hit their retirement targets.

Why may this concept happen?

There are several reasons why many millennials in Australia may never fully retire. Firstly, many are facing significant debts, such as student loans and mortgages, which can make it difficult to save for retirement. The cost of living is also steadily increasing, which means that people have less disposable income to put towards their retirement savings.

Additionally, Australians are living longer than ever before, which means that people will need to support themselves for longer periods of time. While this is great news for those who are healthy and active in their later years, it can pose a challenge for those who have not saved enough to support themselves for an extended period of time.

Working through your older years may be easier.

One way that millennials may be able to support themselves in their later years is by continuing to work. Fortunately, technological advancements have made it easier than ever to work remotely or from home. This means that people can continue to earn an income even if they are not able to work full-time or travel to a physical workplace.

Many people may choose to slow down rather than fully retire, which means that they may continue to work on a part-time or casual basis. This can provide additional income to supplement their superannuation savings and help them to achieve a more comfortable retirement.

High expectations of life experiences and material goods.

Another reason why many millennials may never fully retire is that they have high expectations when it comes to life experiences and material goods. Many people in this age group place a high value on travel, dining out, and other experiences that can be expensive. Additionally, people may be accustomed to a certain standard of living, which can be difficult to maintain on a limited retirement income.

What retirement lifestyle do you want to live?

If you are a millennial who is concerned about your retirement prospects, it is important to take action now. Start by considering what kind of retirement lifestyle you want to live. Do you want to travel the world and enjoy all that life has to offer, or are you happy with a more modest lifestyle?
Once you have a clear idea of what you want to achieve, you can work with a financial planner to develop a plan to get there. This might involve making additional contributions to your superannuation fund, investing in property or shares, or taking other steps to increase your wealth and financial security.

While a fully retired life may not be achievable for many, with careful planning and diligent financial management, millennials can still enjoy a fulfilling and comfortable retirement.

Sources:
https://www.superannuation.asn.au/ *'Superannuation account balances by age and gender', The Association of Superannuation Funds of Australia Limited(ASFA), Ross Clare, October 2017.*

The figures quoted in this article are sourced from the ASFA Retirement Standard, September quarter 2022 report, https://www.superannuation.asn.au/resources/retirement-standard.

Be different today so you can be different tomorrow

Every generation thinks life will be different – and of course, each one is right - but when it comes to planning for the future, while we're young we have a habit of thinking there is still plenty of time. After all, when you're in your mid-thirties or even early forties, retirement is still decades away; later if the government decides so!

However, like anything forgotten too long, the years pass quickly and the time we could have used constructively has disappeared. For example, early Generation X is now on the countdown to retirement.

If you want to be different today, plan to be different tomorrow.

Start with your grandparents…

What did their working life and retirement look like?
Let's imagine your grandparents are both in their eighties. It's likely that Grandad started working in his teens and stayed with one employer for most of his life. Structured superannuation was available to the very few. He retired at 55. Grandma may not have had much paid employment, if any. Their lives can be broken into three phases – education, work and leisure.

But they didn't anticipate retirement being as long as it turned out to be. They're still healthy, have outlived their savings and are relying solely on the age pension to fund their frugal lifestyle.

Then your parents…

What did their working life look like? How will their retirement be different?

We'll envisage your parents are aged in their sixties – typical baby boomers. They were better educated than their parents and both worked; though Mum took years off to raise the kids. They accumulated quite a bit of superannuation; Dad has more than Mum.

Their lives can be broken into the same three phases. Education may have extended into their early twenties or they studied later during their working lives. They worked for a couple of employers and, thanks to technology, ended up in careers they never imagined in their youth.

Whilst they have long talked about retirement, now that it's almost here they face it with some trepidation. They may consider moving to part-time work that will give them more freedom, keep their minds stimulated and still have enough to pay the bills. After all, now they are independent and the mortgage is paid off, life is cheaper.

It would be nice to have more time to travel and do the things they would like to do. They're both fit and healthy and if they live as long as their parents that will be 20 or 25 years of leisure.
Will Mum and Dad have enough money to live a comfortable lifestyle for that long?

And what about you?

You and your siblings are not going to rely on one employer or one lifetime career. Balancing life and work is more important as you take time off to travel, do volunteer work or try new adventures earlier in life. And being so versatile, when you resume your career you simply re-train.

What this means is that you will have multiple periods of education-work-leisure in your life, and as you will probably be much healthier than previous generations you don't see working longer as a problem.

But will you be able to afford 20 or 30 years with no income? That's a sobering thought at any age.

It's time to be different now.

Many social commentators class Generation X as stuck in between the two "noisier" and more well-known generations – Baby Boomers and Gen Y – but that doesn't mean you should fade into insignificance. Be the first generation to truly take control of your retirement at a younger age. Stop the trend and talk to a financial adviser about the many strategies available to give your retirement savings the boost it needs.

Be different today so you can be different tomorrow.

More Australians are unlocking home equity to fund retirement

A growing number of Australians are downsizing their home to fund their retirement. Here's the latest data from the ATO on use of the downsizer measure.

Vanguard's recently released *How Australia Retires* study found that Australians with the highest confidence about their future retirement tend to take the most purposeful action to prepare.

For some Australians that purposeful action to prepare may include selling their principal place of residence at some point with the intention of freeing up extra cash to use during retirement.

The former Turnbull government moved to join the dots between downsizing and retirement five years ago when it commenced the "downsizer measure" from the start of 2018-19.

The downsizer measure enables eligible Australians to sell their home and then deposit up to $300,000 from the proceeds directly into their superannuation account. The measure also enables eligible couples to potentially deposit up to $600,000 from their home sale proceeds into their respective super accounts – $300,000 each.

According to data provided by the Australian Tax Office (ATO), over the period from 1 July 2018 to 30 April 2023 around 58,000 individuals have made downsizer contributions to their super to the value of $14.5 billion.

That equates to an average super contribution size of $250,000 per person from the downsizer measure.
Downsizer amounts are treated separately to standard non-concessional (after tax) super contributions, which allow eligible individuals to make contributions up to $110,000 each financial year or up to $330,000 up-front covering three years.

Downsizing in Australia

Australia's rules around downsizing and super contributions are stringent.

Initially only available to homeowners aged 65 and over, the minimum eligibility age for the downsizer measure was lowered to 60 on 1 July 2022, and then again to age 55 from 1 January this year.

But age is only one of the many criteria that needs to be met to participate in the downsizer measure.

The ATO, which administers the measure, has an extensive list of eligibility criteria (and exclusions) on its website. They include a requirement that a home must have been owned for 10 years or more prior to selling, with ownership calculated from the date of settlement when it was purchased.

The key advantage of making a downsizer contribution into super is that any income earned on that money after age 60 is tax-free in the pension phase.

In the retirement context, downsizing doesn't always involve individuals shifting from a larger dwelling to a smaller one.

Downsizing as a strategy is about extricating equity, primarily for retirement purposes, which may also involve selling a home in a more expensive area and buying one in a less expensive area.

Downsizing in the U.S.

Of course, downsizing for retirement income purposes is not just an Australian phenomenon.

New research from Vanguard in the U.S. examining the strategy of unlocking home equity for retirement purposes has found that among Americans who retire and relocate, about 60% aged 60 and over move to somewhere less expensive.

They typically unlock about US$100,000 of equity from a home they may have purchased decades earlier.

Vanguard researchers analysed millions of migration records from the U.S. Census Bureau's American Community Survey and housing price data from the Federal Housing Finance Agency to determine patterns of relocation around the time of retirement and throughout people's lives.

Interestingly, they found sharp regional differences in how much value can be extracted from a home when a homeowner relocates upon retirement.

While homeowners originating from most U.S. coastal states have the potential to cash out a significant sum, Vanguard found those from the U.S. mid-west and south (with lower median property values) may need to inject principal or take out a mortgage to purchase an average-priced home in the new location.

This home price differential trend is likely to be similar across different housing markets in Australia. For example, there is a large gap between the median property prices in higher-cost capital cities such as Sydney and Melbourne and lower-cost capital cities, as well as across regional areas.

How much equity value can be extracted from a home for retirement income purposes ultimately comes down to prevailing property prices in the selling location, and prevailing prices in the buying location.

Implications for retirement readiness

Vanguard's U.S. researchers found that while it's well-known that home equity represents a significant source of wealth for many American households, how to use it has been less clear in the context of retirement.

Unlocking home equity by relocating to a less expensive housing market can provide a significant source of retirement funding.
"Recent records suggest that this strategy could be thoughtfully deployed by 25% of all U.S. retirees in the next 10 years, potentially significantly improving their retirement readiness," the Vanguard researchers noted.

Australia's downsizer measure effectively opened the door for many Australians to stoke their super balance (either before retiring or after retirement).

People considering making a home downsizer contribution into super – especially those already receiving a partial or full government Age Pension – should do proper due diligence.

Because the Age Pension is calculated on the value of all assets outside of the family home, including the amounts held in a super accumulation or pension account, a large cash injection from home proceeds may result in a breach of assets test rules.

There is a two-year asset test exemption for principal home sale proceeds for people intending to use the proceeds to buy another home. In addition, deemed income (for pension calculation purposes under the income test) on the exempt proceeds is calculated using only a 0.25% deeming rate.

It's important to seek out professional financial advice, especially with respect to social security means testing.

Source:
https://www.vanguard.com.au/personal/learn/smart-investing/retirement/unlocking-home-equity-to-fund-retirement

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A great way to help your kids – and you

We are always hearing about how important it is to insure our own lives and income, but what about insuring our children's?

How would your adult child and their family survive financially in the unfortunate event of an accident or an illness that prevented them earning an income for an extended period of time?

Income protection, TPD and trauma insurance are often not a consideration to a young family in today's financial climate with many struggling with mortgage repayments, education spending and increased living costs.

But what would be your role if your child and their family were suddenly without an income? Without adequate insurance how would they cope?

What if you had helped your child to buy his or her first home and that child suffered a long term-illness or disability? How would that affect you if they couldn't make the repayments?

Here's a scenario...

Alan and Joanne's married son Tim was involved in a car accident, sustaining a spinal injury that prevented him from working for two years. Unfortunately, Tim did not have income protection or accident insurance.

The bank foreclosed on his mortgage and Tim and his young family were forced to move in with Alan and Joanne. Eventually, Tim recovered and was able to return to work.

Aside from the emotional impact on Tim and his family, Alan and Joanne's retirement plans were seriously compromised. Joanne's health deteriorated due to the extra stress of the situation and she was diagnosed with severe depression.

What could Alan and Joanne have done differently?

They could have asked Tim if his income was protected in the case of an unforeseen illness or injury.
Learning that the young couple was allocating all spare cash to the mortgage, the parents might have offered to help pay for adequate insurance cover.

Even if you are not in a position to contribute to the cost of their insurance, raising the issue with your adult children and encouraging them to talk to a financial professional could be some of the best guidance you could ever give them.

New financial year means you may be eligible for Commonwealth Seniors Health Card

The new financial year has begun, which means you might now qualify for a Commonwealth Seniors Health Card (CSHC).

The CSHC is a means-tested card that provides concessions on health-related costs for eligible seniors.

Those who already have a CSHC, and are still eligible, will receive a new one by the end of September. It will be valid for up to two years, expiring at the end of your birth month. From then on, you'll be sent a new CSHC every two years before your old one expires.

The card gives you access to cheaper medicines and medical bulk billing, as well as several other state and federal concessions.

The CSHC explained

The CSHC is not the same as a Health Care Card or a Low Income Health Care Card, even though those concession cards are also issued by Services Australia. Those cards have different eligibility requirements and income tests to the CSHC.

The CSHC is a concession card that delivers cheaper healthcare and some lifestyle discounts if you've reached Age Pension age. Cards are issued at the start of the financial year.

You have to apply for the CSHC, and it is a separate application than a claim for the Age Pension.

As the CSHC is income based, it means that you are able to use the (projected) income from this *current* financial year as a basis for your claim, if it is likely to bring you under the threshold.

Are you eligible for a CSHC?

You can apply for a CSHC if you meet these requirements.

You must have reached Age Pension eligibility age

The current eligibility age for the Age Pension as of 1 July 2023 is 67, after being lifted from 65 in six-month increments progressively since 2017.

You must live in Australia and meet the residence rules

You'll need to be living in Australia when you claim a CSHC and must be an Australian citizen, hold a permanent visa, or hold a Special Category Visa as a New Zealand citizen living in Australia. You must continue to meet the residence rules the whole time you are using the CSHC.

Most newly arrived residents have to wait two to four years before being eligible for the CSHC. You must satisfy residence rules while you're using the card.

You must provide a Tax File Number (TFN)

You'll need to provide Services Australia with your TFN or be exempt from doing so.

Meet the identity requirements

You will need to prove your identity to Services Australia before you are entitled to receive a CSHC.

If you are claiming a benefit from Services Australia for the first time, you need to provide an acceptable photo identity document (such as drivers' licence or passport) in person at a service centre. Otherwise, you will need to provide your existing Centrelink Customer Reference Number (CRN).

Your income must fall under the annual CSHC income threshold

The CSHC income threshold is different to the Age Pension income test. There is no assets test for the CSHC and assets such as your family home are not counted.

To meet the income test, the assessable income must be below the following thresholds:

- $90,000 for singles
- $144,000 for couples
- $180,000 for couples separated by illness, respite care or prison.

If you are caring for a child, you can earn an extra $639.60 per year.

You may be eligible for a CSHC even if you are no longer receiving a pension because of changes to:

- your income and assets
- the pension assets test.

You may also be eligible for a CSHC if you are widowed or separated from a partner who receives either:

- Age Pension
- invalidity service pension.

If you already have a Pensioner Concession Card (PCC), you will not be eligible for a CSHC.

Account-based income streams

Services Australia assesses your Account-BasedPension as part of the income test and includes account-based annuities.

The balance of your Account-Based Pension is subject to deeming, which assumes investments are earning a certain rate of income.

Deeming rules will only apply if any of the following occurs:

- you bought or changed it on or after 1 January 2015
- you own it and were granted your Commonwealth Seniors Health Card after 31 December 2014
- your partner owns it and they are 60 years old or more.