Financially speaking

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Macro Perspectives: Recession, inflation and duration consideration

Author: Stephen Dover, CFA, Chief Market Strategist, Franklin Templeton Institute

From a macroeconomic perspective, 2022 centered around the actions of reserve banks around the world. While the fight against inflation continues into 2023, the discussions are more focused on recession and potential weakness in the US Dollar. I recently gathered with some of our economists across the firm to discuss these topics – here are some of my key takeaways:

- **US inflation is trending lower, but the fight isn't over yet.** This contrasts with Europe, where inflation remains higher and has not peaked. Asia has generally seen milder inflation. Japan, for the first time in over 20 years, is experiencing inflation and positive real interest rates. Our economists disagree on how quickly and how far inflation will fall. The market consensus suggests US inflation will run at roughly 3% for the full year. Internally, we have a healthy debate on how quickly inflation will fall and whether it will get to the US Federal Reserve's (Fed's) 2% target.
- **Interest rates are near peaking.** In the United States, we expect the Fed's policy rate to rise to at least consensus expectations of around 5%, with the possibility of reaching 5.25%. Our economists disagree on how long the Fed will hold rates at the higher level. The implications for fixed income and equity investors are that the Fed is unlikely to provide a "Fed put" if the market has a correction.
- **How deep might a US recession be?** One could describe 2023's economic outlook as "the most-anticipated recession ever," with surveys of economic forecasters and market behaviour in 2022 providing the evidence. Everyone seems to "know" the United States is going to have a recession, and everyone seems to "know" it will be mild. Whenever "everybody" thinks something, that type of herd mentality makes me nervous because often the herd is misguided. I gain some comfort from internal discussion and healthy debate among our economists, whose views on recession vary from the possibility of no recession at all, to a "normal" recession, which typically lasts about 10 months.

LeenaneTempleton wealth management

Leenane Templeton Wealth Management Pty Ltd
A Corporate Authorised Representative of LT Advice Pty Ltd
ABN 21 637 033 286 | Australian Financial Licensee 523026

484 Hunter Street
Newcastle NSW 2300
T: (02) 4926 2300
W: www.LT.com.au
E: info@LT.com.au

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- **Time to consider increasing fixed income allocation.** Fixed income is now providing income again. Rates are near a peak, and 2023 may be a year of positive returns for fixed income. We see a general shift toward larger fixed income allocations no matter how one is currently positioned.
- **There's a quality bias when leaning into fixed income.** We believe investment grade and sovereigns are particularly attractive in this environment, with continued economic uncertainty perhaps providing opportunities on a selective basis in areas like high yield.
- **Opportunity outside of the United States.** This year, analysts expect US growth to come in below that of Japan – which has not happened for over two decades – while emerging and developed Asia overall will likely see higher growth than the United States. Meanwhile, Europe's economy is doing better than many forecasts expected, due largely because of a mild winter.
- **Expect volatility.** While our economists agree that taking a long-term strategic view suggests taking on a bit more duration, there may be tactical opportunities within the fixed income markets.
- **Emerging markets may have tailwinds.** Both debt and equity markets in emerging markets are seeing favourable conditions. Relatively stronger growth rates combined with tempered inflation – and the potential US Dollar may have peaked – provides opportunities, particularly in Asia.
- **Asia generally, and specifically Japan and China, may provide new opportunities for active investors.** With a whiff of inflation in Japan, it is now facing different dynamics than during previous decades of deflation. Meanwhile, China is finally coming out of COVID-19 lockdown, which should help spur renewed consumption and improve global growth prospects.

These are my main observations as we lean into 2023. The table below explores some of these issues more deeply from the lens of the economists across Franklin Templeton.

Wild cards: Worries and optimism

Here are some key themes our economists are watching closely.

US debt ceiling/budget deficits

Government deficits around the world have grown since pre-COVID. We are mindful of economic and market risk if the United States does not resolve its debt-ceiling limit. This could cause severe market volatility, and in the worst case, could lead to a ratings downgrade.

"Sticky" inflation

If the global economy is stronger than expected, and inflation proves more long-lasting, this could cause a very different monetary policy approach (tighter for longer) than the market is currently pricing in.

Growth in Asia and China's reopening

With China beginning to reopen, growth dynamics could have some moderate inflationary impacts.

The recognition that Asia's growth rate is likely to outperform that of the United States' is not without country-specific risks, but also creates opportunities for investors in non-dollar assets.

Europe, energy and war

Amid a milder-than expected winter, Europe seems unlikely to face the type of severe downturn feared just a few months ago. The outlook can be considered fairly encouraging, but still represents geopolitical uncertainty, especially as the Russia-Ukraine war continues.

A Will isn't always the only way

You would have heard the saying: "where there's a will, there's a way". This statement is usually used to encourage people who are losing enthusiasm for a task or goal.

But it also reflects the way many people feel about estate planning. They think that so long as you have a Will, you have a way to ensure your wealth is passed correctly to your loved ones. But this is not necessarily the case.

The truth about Wills

A Will can help ensure the assets that form part of your estate are distributed according to your wishes.

But did you know that a Will typically only applies to personally held assets and therefore may not deal with a significant portion of your wealth?

For example, the proceeds from your superannuation funds and life insurance policies don't necessarily form part of your Estate. They can pass directly to certain beneficiaries, who may have been nominated by you, or go to your Estate where they'll be dealt with by your Will.

Also, some assets never form part of an estate, like jointly owned assets or assets held in a discretionary family trust.

To cover all bases, thorough estate planning (or personal succession planning as it's also known) involves putting in place strategies that address all your assets, not just those covered by your Will.

Do I need a personal succession plan?

Just about every asset you own and every investment you make has estate planning implications. As a result, personal succession planning is something everyone needs to consider, regardless of age or stage in life.

At a minimum, every individual should have:

- a current Will to distribute estate assets
- an Enduring Power of Attorney to cover situations where they're unable to make financial decisions themselves
- appropriate superannuation and insurance beneficiary nominations, and
- appropriate arrangements in place to distribute or pass control of any assets that are not covered by the Will.

What are the benefits of personal succession planning?

Personal succession planning can:

- provide certainty by getting the right assets in the hands of the right people, at the right time
- enable you to provide for and protect your loved ones while reducing tax payable by your beneficiaries, and
- provide certainty that your children are taken care of.

What are the consequences of NOT having a personal succession plan?

Personal succession is something you should address now. Don't wait until it's too late. If you die without a valid Will, intestacy legislation will determine how your estate assets are distributed among your surviving family members.

If you die without a valid superannuation or life insurance death benefit nomination, the proceeds may not be distributed according to your wishes.

And, if you're badly injured in an accident or lose mental capacity, who will manage your affairs while you're still alive but unable to make your own decisions?

How we can help

With assistance from legal and tax professionals where appropriate, we can:

- Ensure you're making the right ownership decisions when acquiring new assets or re-structuring your existing assets. For example, we can help you determine whether it's best to invest in your name, your partner's name, or jointly with your partner. We may also identify whether further tax and legal advice is required to consider another ownership arrangement, such as a trust, is appropriate.
- Determine if you have sufficient means to achieve your estate planning objectives. Additional life insurance inside or outside of superannuation may be necessary to provide your family with a lump sum payment or an income stream to repay debts, meet their ongoing living expenses and cover your children's future education costs upon your death.
- Develop a range of strategies to provide certainty, tax efficiency and/or asset protection. For example, we can explain superannuation death benefit and life insurance beneficiary nomination options. By making appropriate nominations now, your beneficiaries will be able to effectively and efficiently receive the death benefit when you're no longer around.

We can help you address these and other estate planning issues as part of your broader financial planning.

Centrelink assistance for working age pensioners and incentives to downsize your home

There have been positive Centrelink changes to incentivise pensioners to increase their participation in the workforce (amid staff shortages) and to downsize from their family home.

$4,000 Work Bonus increase

The Work Bonus provides senior Australians with an incentive to continue working at least on a part time basis, by providing an exemption to income from work.

How it works

Under the Work Bonus, the first $300 of fortnightly income from work is not assessed under the pension income test. Any unused part of the $300 fortnightly Work Bonus accrues in the Work Bonus income bank and can be used to offset future income from work.

On 1 December 2022, a one-off $4,000 income credit was added to the Work Bonus income bank of those at least pension age and in receipt of an Age Pension, Disability Support Pension, Carer Payment or certain Veterans entitlement.

Prior to 1 December 2022, the Work Bonus income bank was capped at $7,800. This has been temporarily increased to $11,800 until 31 December 2023. Effective 1 January 2024, any amount in the Work Bonus income bank that exceeds $7,800 will be lost and not available to offset future employment income.

Case study

Mary is an age pensioner who works for three consecutive fortnights as an accountant. She has no other income. As Mary has not worked in the previous 12 months, she has accumulated the maximum income bank amount of $7,800 (26 fortnights x $300). Since 1 December 2022, her income bank was credited with $4,000, which brings her total income bank to $11,800 ($7,800 + $4,000).

During the three fortnights that she works, Mary earns $3,000 a fortnight, a total of $9,000. As Mary's income bank amount is more than her employment income, none of the $9,000 is assessed under the income test and so her work income does not reduce her age pension.

In contrast, without the additional $4,000 credit to her income bank, her age pension may have been reduced due to her work income.

For income tested pensioners (eligible for the Work Bonus), those earning:

- more than $300 per fortnight may see a temporary increase in entitlements, and
- less than $300 per fortnight may consider temporarily taking on additional paid work without impacting their Centrelink entitlements.

Centrelink incentives to downsize your home

Pensioners are often concerned about downsizing their existing home, where the sales proceeds may become assessed towards their assets and income test and negatively impact their age pension (previously their home was exempt from assessment while they lived there).

To encourage pensioners to downsize, in conjunction with the Super downsizer contributions law, the Government has

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legislated to enhance the Centrelink concessions applicable to pensioners who sell their existing home and intend on applying a portion of those proceeds to purchase, build, repair or renovate a new home.

Since 1 January 2023, the asset test exemption period has been extended to 24 months (from 12 months). The exemption only extends to the amount that is intended to be used for these purposes. For example, if a pensioner is downsizing and only 75% of the home proceeds will be utilised for the new home, the assets test exemption is limited to this amount.

Exempt proceeds that are held in a financial investment, such as a bank account, will be subject to the income test via the lower deeming rate only (currently 0.25%) during the exemption period. They are also isolated from other financial assets which may be deemed at the higher deeming rate of 2.25%.

Please seek further advice from your Financial Adviser.

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What is the value of life insurance?

Life insurance can be valuable at various life stages, whether you're young and single, starting a family or transitioning to retirement.

What is life insurance?

Adequate life insurance can help provide financial security for you and your family through a lump sum payment if you were to be diagnosed with a terminal illness or pass away. It can also give you peace of mind that your family will be looked after and will have financial protection if you were not around. Life insurance can be of help at every stage of your life. Let's discuss some of the scenarios where life insurance can be valuable.

Major health concerns among Australians

Cancer is one of the biggest health concerns for Australians. According to the Cancer Council, at current rates, 1 in 2 Australians are expected to be diagnosed with cancer by the age of 85.[1] The high prevalence of the disease among Australians should give you pause for thought about protecting your family in case the unexpected happens. However, it's not only those with health concerns who should consider life insurance. Even if you're young, fit and healthy, starting a family or planning your post-retirement life, life insurance may have some benefit for you.

Young and single

When you're young, single and healthy, life insurance is probably the furthest thing from your mind. After all, you're in the prime of your life and have other expenses to think about. But life can be unpredictable, and it doesn't hurt to plan ahead. If something unforeseen were to happen, would your immediate family be able to cover your existing loans and expenses? What's more, you may be able to get a better premium if you're able to lock in your policy while you're young and healthy, as opposed to when you're older and have other health complications.

Married or starting a family

When you get married or think about having kids, you have other dependents who will now rely on your income. It can be a good time to consider life insurance to provide them with a financial safety net if the unthinkable happens. So, they're not left struggling to keep up with mortgage, childcare payments or everyday expenses in your absence.

Transitioning to retirement

It's a misconception that life insurance is only about giving a lump sum payment to your family or loved ones in the event of your death. It's much more than that. When you're older and transitioning to retirement, life insurance can give you the financial freedom to live life on your terms, knowing that your family will not be under financial stress to pay bills or even your funeral costs.

Get professional help

If you'd like further information please speak to your **LT** Financial Adviser.

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[1]www.cancer.org.au/cancer-information/what-is-cancer/facts-and-figures

Important Information: Source: TAL. Any advice is general in nature only and has been prepared without considering your needs, objectives or financial situation. Before acting on it you should consider its appropriateness for you, having regard to those factors. Persons deciding whether to acquire or continue to hold life insurance issued by TAL should consider the relevant Product Disclosure Statement (PDS). The Target Market Determination (TMD) for the product (where applicable) is also available. Life insurance issued by TAL Life Limited ABN 70 050 109 450 AFSL 237848.

How to do a daily digital detox

Australians spend more time scrolling than sleeping. Here's how to take time to recharge yourself.

Do you ever feel as if life is just speeding by and you're running from one thing to the next, without time to pause and regroup? You're not alone. Despite all the technology we have in our lives that in some way saves us time, it often seems that we are more stressed and time poor than ever before.

This is not 'news'. A Medibank study found that Australians are spending an average of nine hours a day looking at computers, TVs, smartphones and tablets. That's more time than we're spending sleeping!

Eye strain headaches, posture issues, fatigue at work, lack of sleep and lack of physical activity are just a few possible side effects of our busy, technology-focused lives. We all know it would be good for us to cut back on the time we spend on our digital devices. And yet, so many of us are not taking the steps we need to slow down and reboot ourselves each day.

Wellbeing isn't just about exercise and diet. A big part of wellness is mindset and mental clarity. To achieve this, it's important to get back to basics with three core pillars of vitality: fresh air, fresh food and a fresh perspective.

Taking regular breaks away from your laptop, phone, tablet and TV can help you to reconnect with your surroundings, create a pause of mental clarity and creativity, and give you a chance to notice your posture and your breathing.

Tips for giving yourself a daily reboot

During the day

- Place a sticky note on your computer that says "Take a nano break" and make a point of getting up and walking away from your computer for a few minutes. Go talk to a colleague personally rather than emailing across the room.
- Try to stay off Facebook and social media in the morning before work. Listen to music or a podcast or read a book instead.
- Take a fresh air break at lunchtime, rather than eating lunch with your phone or iPad in front of you. Look up, look around.
- Plan to do some physical activity most weekends away from your devices. Use this time away from work to recharge your mental and physical batteries.

At night

- Avoid TV, illuminated alarm clocks and other digital stimuli in the bedroom.
- Read a book before you go to sleep, rather than watching television or working late on the computer.
- Meditate and concentrate on breathing. Channel your thoughts from worry to a place of peace.
- Create a regular bedtime routine and a regular sleep-wake schedule.
- Create a restful environment that is dark, cool and comfortable. Play restful music to help you relax.
- Keep a diary of things that are on your mind, even if it's just a list of things to do for the next day. Get them out of your head and onto paper.
- Think of a digital detox as recharging your own batteries. If we do not fully recharge our batteries, then we diminish our energy levels and our ability to handle stress and perform daily tasks.

After you've read this, rather than stay on your phone or connect to Netflix, why not lace up your shoes, head out the door or get up and have a chat with a friend or family?

Sometimes you need to disconnect to reconnect.

Source: Medibank. Written by Nikki Fogden-Moore, specialist in private coaching for high achievers to bring business and personal vitality to life. While Medibank hope you find this information helpful, please note that it is general in nature. It is not health advice, and is not tailored to meet your individual health needs. You should always consult a trusted health professional before making decisions about your health care. While we have prepared the information carefully, we can't guarantee that it is accurate, complete or up-to-date. And while we may mention goods or services provided by others, we aren't specifically endorsing them and can't accept responsibility for them. For these reasons we are unable to accept responsibility for any loss that may be sustained from acting on this information (subject to applicable consumer guarantees). ABN 47 080 890 259.

Thinking ahead? Let's talk about strategies for creating a positive financial future. **LT.COM.AU**

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