March 2022

Welcome to the latest edition of our newsletter,

Our articles cover a range of topics which we hope you will find interesting. We aim to keep you informed of changes as they happen, but we also want to provide ideas to help you live the life you want – now and in the future.

In this edition we discuss

* Why Australian interest rates are likely to rise and when
* 9 money tips if you're having a baby
* Living costs for retirees rise at fastest pace in 10 years

If you would like to discuss any of the issues raised in this newsletter, please don't hesitate to contact us.

In the meantime we hope you enjoy the read.

All the best,

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Why Australian interest rates are likely to rise and when

Senior economist Diana Mousina answers our questions on potential interest rate changes and what it could mean for Aussie households.

Why have interest rates been so low for so long?

The main reason interest rates have been kept so low is the Reserve Bank of Australia undershooting on its inflation target of 2-3%. We haven't seen underlying or core inflation within that band sustainably since before 2014.

As well as inflation, a few other factors have kept growth in Australia below trend over the past decade—even before the pandemic.

Mining investment peaked back in 2012 and then after that there was a period of weaker GDP growth. Wages growth has been pretty low as well at about 2% annually when normally it should be closer to 3%.

And there's also been spare capacity in the labour market with the unemployment rate, while not super high, probably more elevated than the RBA would like.

All these factors have kept downward pressure on rates, in line with the general experience across developed countries.

Do you think interest rates will increase in 2022?

AMP's view is that interest rates will increase in 2022 for the first time in over 10 years. At the moment we think the first hike will probably be in August and another one in September, and by the end of the year the RBA cash rate will be up to 0.5% from 0.1%.

An earlier rate hike is possible and the earliest it could probably happen is around June. May is complicated by the upcoming federal election as the RBA usually tries to steer clear of any perception it's influencing political outcomes. So they'll probably try to wait until the election's out of the way and also see what's in the Federal Budget, although this could be a little redundant if there's a change in government, which appears to be a distinct possibility if you believe the betting odds.

It's important to remember that even if we do get interest rate hikes this year, the cash rate will still remain pretty low. Next year we expect more rate hikes to take the cash rate to between 1.25% and 1.5% by the end of 2023.

What are the main factors the Reserve Bank will take into account when deciding whether to raise rates?

Like most central banks around the world, the main issue here is inflation, which has been running at a much higher than expected pace.

There are a few reasons for this. The pandemic is causing disruption to supply chains and that's leading to increases in the price of transporting goods and higher commodity prices.

There's also been a huge increase in monetary and fiscal stimulus over the past two years, boosting demand for goods and contributing to higher prices.

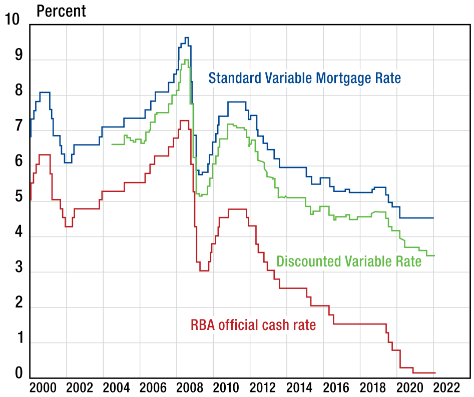
While the supply chain issues are probably not going to last for ever and should start to ease off by the end of this year, it looks like the price of goods has shifted on a more long-term basis (from higher demand) and services inflation will rise as spending gets back to pre-Covid levels. As a result, we think inflation will be persistently higher than it has been over the past few years.

As well as inflation, the RBA is also looking very closely at the lower unemployment rate and signs that a pickup in wages growth is likely this year.

What do changes in interest rates mean for Australians?

As you can see in the following graph, variable mortgage rates tend to follow the RBA cash rate so an increase in official cash rates will probably mean higher variable rates for mortgage holders.

Australian mortgage rates



Source: Macrobond, AMP Australia

And of course, even if you're on a fixed interest rate for your home loan then when you roll over to a variable rate your interest rate will be higher.

So this is certainly something to take into consideration when you're looking at your budget over the next few years.

But we think in this overall cycle any rate hike will be limited to around 200 basis points, or 2%, so we should keep it in perspective. Banks usually make sure there's a buffer of about 2.5% when they look at serviceability of a new home loan and that's been increased recently to 3%.

So even a 2% rate hike should be pretty sustainable for the majority of households. Naturally, like any rate increase it will probably lead to weaker home price growth and weaker consumer spending but it's unlikely to be enough to cause a severe downturn in the Australian economy.

People get this idea that an interest rate hike is the end of the world. But any increases should be gradual and overall rates aren't likely to go up by anything more than 1-2% over the next few years. And hopefully we'll get some wages growth to offset the pain.

9 money tips if you're having a baby

Having a baby is a wonderful thing, but it can also mean big changes to your lifestyle and finances, particularly if you consider that parents with children under age 12 fork out around $18,200 a year on basic expenses[i].

With that in mind, if you're expecting a baby or planning on having one, here are some tips to help you budget and save.

1 Make sure you're across medical expenses

Medical costs might include ultrasounds, birthing classes, special tests, vaccinations, and check-ups, so it's worth jotting these down, so you've got an idea of everything that could be coming up.

You'll also want to consider whether you want to have your baby in a public or private hospital, as there may be out-of-pocket expenses with either option, even if you have Medicare or private health insurance.

Many private health funds also have waiting periods before you can claim on pregnancy and birth-related costs, so if this is something you're considering, you'll want to look into this early.

Meanwhile, if you want your child to be covered under a health insurance policy, you may need to do some investigating, as a single or couple policy may need to be extended to a family policy.

2 Consider other upfront and ongoing costs

There are things you may need to buy before the baby arrives, in addition to other things you might need on an ongoing basis. This might include things like a car seat and stroller; cot and mattress; maternity clothes, baby clothes and baby bag; food, nappies, bottles and formula and childcare.

3 Research your employer entitlements

Many organisations have their own parental leave policies, which may include various paid and unpaid parental leave entitlements for new mothers and fathers.

If you're unsure, speak to your employer to see if there is a scheme in place and find out what they offer as part of this. At the same time, you may also want to find out if you're eligible for any annual leave, long-service leave, or regular unpaid leave, if you're planning to take time off work.

When you're speaking to your employer, it may also be helpful to check the company policy around superannuation. Super generally isn't paid when you're on parental leave, so you might want to consider whether you'll make additional contributions while you're still working.

4 Explore the government's paid parental leave scheme

With the paid parental leave scheme, primary carers of newborn or adopted children can apply for parental leave payments from the government, which provides the national minimum wage for up to 18 weeks[ii].

These payments can be received in addition to any payments your employer pays under its own parental leave policy, if you're eligible.

You can also apply up to three months before your child's due date, which may help you to better prepare for your time off, as you'll be able to choose when your paid parental leave period starts[iii].

5 Investigate other government assistance options

Beyond the paid parental leave scheme, there's a range of additional support options for families.

You may be entitled to other assistance such as Dad and Partner Pay, which provides up to two weeks of government-funded pay, or the Family Tax Benefit, which helps with the cost of raising children.

The Child Care Subsidy also provides assistance with childcare fees for eligible families. From 7 March 2022, families with more than one child aged five or under (in childcare) will also get a higher subsidy for their second child and younger children[iv].

6 Create a family budget with the information you've collected

After you've considered the expenses, as well as any entitlements you may be eligible for and how long you may take off work, it's worth drawing up a budget and starting to put some money aside.

When you do this, take into account any existing day-to-day expenses you might have, such as utility bills, groceries, petrol, insurance, rent or home loan repayments, and other debts you might be paying off.

You may also want to factor in any additional sources of income (such as investments), and whether you have family that may be able to assist in helping you minimise expenses.

7 Prioritise your existing debts if you can

If you have existing debts, like credit cards, personal loans or a home loan, you may want to consider how you can reduce these debts as much as possible before the baby arrives, particularly as you may encounter other unexpected expenses along the way.

8 Consider your will and broader estate plan

If a little person is about to enter your life, who you want to take care of, thinking about your estate plan may also make good sense, noting this involves more than just drawing up a will.

It'll include decisions around who will look after you, and your child, if you're ever in a situation where you can't make decisions for yourself, as well as documenting how you want your assets (which may include insurance and super) to be distributed should you pass away.

9 Remember that money isn't everything

If it's your first baby, while it may be tempting to invest in the most expensive pram, baby clothes, or day care centre for your little one, it's the love for your child, not the amount you spend on them, that matters.

i Finder – The cost of raising kids 2021
ii Services Australia – Parental Leave Pay
iii Services Australia – Claiming timeframes
iv Child Care Subsidy – Higher Child Care Subsidy and removal of annual cap

Living costs for retirees rise at fastest pace in 10 years

We look at how much money you might need each year and ways you can still budget for your social life.

Australian retirees generally need a certain budget each year to live a modest or comfortable lifestyle, and industry figures recently revealed the highest annual increase in those budgets since 2010[i].

The Association of Superannuation Funds of Australia (ASFA) put that increase, in part, down to a range of unavoidable price hikes on things such as petrol and council rates[ii].

If you're in or approaching retirement, that mightn't be welcome news, particularly if you're prioritising bills, trying to reduce debt, helping the kids out (if you have any) and enjoying an active social life.

On the flip side, knowing how much you might need and what you may like to do could go a long way.

So, how much money do you need?

According to September 2021 ASFA figures, individuals and couples, around age 65, who are looking to retire today, would need the below annual budgets to fund certain lifestyles[iii].

Figures are based on the assumption people own their home outright and are relatively healthy[iv]. You can also see how these budgets compare to the current maximum Age Pension rates being paid by the government[v].

	Comfortable lifestyle	Modest lifestyle	Full Age Pension rate
Single (annual budget)	$45,238	$28,775	$25,155
Couple (annual budget)	$63,799	$41,446	$37,923

Note, a comfortable retirement lifestyle is said to enable an older, healthy retiree to be involved in a broad range of leisure and recreational activities, whereas a modest lifestyle involves just basic activities[vi].

How much are you likely to spend on recreation anyway?

According to figures, singles and couples around age 65, living a comfortable lifestyle in retirement, would spend about $189 and $285 of their weekly budget respectively on leisure and recreation, whereas singles and couples living a modest lifestyle would spend about $97 and $153 respectively[vii].

This takes into account recreational activities like[viii]:

- Movies, plays, sports and day trips
- Lunches and dinners out
- Club memberships
- Takeaway food and alcohol
- Streaming services like Netflix and Stan
- Domestic vacations (and for those living comfortable lifestyles, international ones too).

What activities are on your to-do list?

Considering the above figures, it may be worth thinking about what you enjoy doing or what you're likely to want to do more of with extra time on your hands.

These things may include:

- Sport – golf, tennis, cycling, yoga, pilates
- Hobbies – fishing, sailing, photography, drawing, woodwork
- Club associations – Rotary, Leagues, Surf Life Saving
- Tournaments – trivia, bridge, chess
- Eating out – restaurants, beach barbecues, picnics, food fairs
- Travel – interstate breaks, overseas holidays, road trips, caravanning
- Entertainment – cinemas, concerts, events, stage shows
- Volunteering – hospitals, soup kitchens, animal shelters.

Making your money go further for the fun stuff

The good news is, not all things will come with a price tag, so it will be possible to do a variety of things that don't necessarily cost money.

In the meantime, here are a few simple things that you might consider to keep costs down in retirement.

- Make use of your Senior's Card for transport concessions and discounts on other goods and services
- If a restaurant isn't in your budget one week, pack a rug, basket and esky, and head out for a picnic
- If you enjoy dining out, research cheaper deals on sites like Groupon and Scoopon
- Have your friends over for a card night or take turns hosting simple dinner parties where people BYO
- If you want to get away, look out for cheap flights or consider a road trip. There are lots in Australia
- Find cheap accommodation on Airbnb, HotelsCombined, lastminute.com or consider listing your own place to earn some money while you're away.

If you would like to discuss your plans for retirement, please don't hesitate to give us a call

i, ii ASFA media release – Living costs for Australian retirees rise at fastest pace in a decade – November 2021

iii, iv, vi ASFA Retirement Standard – September 2021

v Services Australia – Age Pension – How much you can get – 2 February 2022

vii, viii ASFA Retirement Standard - Detailed budget breakdowns – September 2021, page 3