



## Crunching the numbers on transition to retirement

Transition to retirement or TTR is now a well-accepted and financially positive way to smooth the path from the workforce into retirement. In simple terms, a TTR allows you to maintain your 'in-pocket' income but change the mix. You can use your super account to start a new income stream, while at the same time topping up your super account by increasing the amount of salary you 'sacrifice'.

However, changes in the 2012 Federal Budget raise an important question. Has the reduction from \$50,000 to \$25,000 in the amount that can be contributed at the concessional tax rate now reduced the benefits of a TTR strategy for some people?

### How it works

Under the 'Transition to Retirement' rules, people aged 55 or over can access their super while still working. Some or all of their super is rolled into a 'non-commutable' income stream which pays them a regular income, often referred to as a pension. However, this does not allow them to withdraw a lump sum.

With this pension income stream, they then have the option to salary sacrifice more of their earnings into super while maintaining their overall income level. Because salary sacrifice uses before-tax dollars, it may be possible to contribute more to super than is actually withdrawn.

### 2012 Budget changes

From 1 July 2012 everyone has a maximum concessional contribution cap of \$25,000, regardless of age. The move halves the cap for people 50 and over, possibly affecting the option to use salary sacrifice in the transition to retirement strategy.

But it is not just budget changes that impact on TTR. People's circumstances change all the time. Changes to the balances of people's superannuation accounts and their need for income make it necessary to regularly review your retirement strategy with a professional.

### Three key benefits of a TTR<sup>1</sup>

Firstly, superannuation savings are moved into pension phase and tax no longer applies to the investment earnings, including realised capital gains. This boosts the effective earnings rate.

A second benefit is that money can be withdrawn from preserved benefits as pension payments, which can help increase disposable income. Using this approach may support a move to part-time work or allow an increase in home loan repayments to further reduce debt before retirement.

Finally, salary sacrificed income can be replaced with pension income. For someone aged 60 and over this can provide personal tax savings. For someone between 55 and 60, there may be some savings if less income is taken out than is sacrificed back into super.

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## Crunching the numbers on transition to retirement continued

The first two benefits are not impacted by the change. However, the third advantage, the ability to create personal tax savings, may be reduced.

### Jane's strategy

Jane is aged 55 and earns \$82,000 from her employment. Her net income is \$62,480\* in 2011/12 (\$62,483 in 2012/13). Her employer contributes \$7,380 under the Superannuation Guarantee.

Jane has \$350,000 in super (all taxable component), generating taxable income in the fund of 5 per cent per annum. In 2011/12, Jane salary sacrifices into super up to her limit of \$50,000 and draws enough money from a TTR pension to maintain her net income.

In 2012/13, her contribution limit comes down to \$25,000 so Jane talks with her adviser to see if it is worth continuing the strategy. When they go through the figures, the calculations show there will be some significant differences between the two financial years.

For example, the amount Jane can salary sacrifice is cut by \$25,000 but the amount of pension she draws from

super also falls significantly. Her personal tax bill rises but her contributions tax falls by nearly as much, leaving her with about half the tax saving on income that she could achieve in 2011/12, a drop of around \$700. However, the tax saving on investment earnings is unchanged from 2011/12 to 2012/13.

And the bottom line is what is important to Jane and her adviser. This shows clearly that while the strategy may be less effective after 1 July 2012, it will still generate valuable savings from the lower tax on investment earnings.<sup>2</sup>

### Impact on the 60 and over

The story is a similar one for an employed person who is age 60 and over. The value of the strategy is significantly reduced from 1 July 2012 but some benefit remains, and the end result is usually better than doing nothing.

### Creating your future

TTR strategies can help you build an effective base as you move into retirement so it is important to sit down with your adviser to work out the numbers that apply to your situation. There are a lot of factors to consider but in most cases the value of a



TTR strategy depends on tax savings on the investment earnings, as well as the amount you have available to salary sacrifice.<sup>3</sup>

We can help you to review your strategy, to monitor it, and to make adjustments in light of changes in the rules or your own personal circumstances.

<sup>2</sup> 'Is TTR still effective?', [www.strategysteps.com.au](http://www.strategysteps.com.au)

<sup>3</sup> *ibid*

## Export lows and dollar woes may not be all bad news

**A year-long slowdown in Chinese imports of iron ore and coal had resulted in lower prices long before the Eurozone debt crisis escalated. Obviously these setbacks must affect the Australian economy – but how serious and long term will the impact be?**

### China's demand has slowed, but not stopped

Jin Liqueur, Head of China's Future Fund, explained that the country's economy was deliberately slowed down over the past year to reduce inflationary pressures and a domestic property bubble. However, there is now some concern that the slowdown went further than expected because the Eurozone crisis shrunk China's European export markets, prompting predictions of a government stimulus package.

Of course, the Chinese economy remains impressive – even in a slow period. In the first quarter of 2012, its growth dropped to a low of 8.1%, compared to 2% for the US and 1.7% for Germany.

### Miners continue to invest in Australia

Both iron ore and coal prices have dropped in the past year, but at the same time our biggest miners continue to invest heavily in Pilbara iron ore and Queensland coal and both Rio Tinto and BHP believe the iron ore

market will be strong for the next decade. While reinvestment of profits is a sign of the health of an industry, for the country it means a continuation of our two speed economy.

### Both the Australian dollar and interest rates are down

The Australian dollar continues to dance around parity with the US dollar, but has fallen from its recent highs, and the Reserve Bank has dropped the official interest rate – both largely outcomes of Eurozone instability.

The lower Australian dollar may be bad news for local online shoppers, but it is certainly good news for our exporters, including the miners and for our tourist industry.

Similarly, lower interest rates should please commercial lenders and industrial borrowers, but will not be welcomed by investors who sought shelter from the financial storm under a fixed interest umbrella.

Income investors who are feeling the pinch may wish to explore alternatives such as managed bond funds that include higher



interest corporate bonds, or even a cautious return to the share market via dividend stocks with fully franked tax benefits.

If you would like to discuss these or any other current issues, please contact us.

<sup>1</sup> <http://www.smh.com.au/business/chinas-economy-slows-more-than-expected-20120413-1wxt8.html#xzz1yJGS8qmY>

<sup>2</sup> <http://www.economist.com/blogs/analects/2012/05/chinas-plans-growth>

<sup>3</sup> <http://tradingeconomics.com/gdp-growth-rates-list-by-country>

<sup>4</sup> SMH Business Day, 22.6.1, page 1: Rio reaping reward of North move.P7.“Both believe steel production and underlying iron ore demand will be strong for the next decade”.

<sup>5</sup> <http://www.morningstar.com.au/funds.mvc/article/australian-euro/4864/>

## Helping women plan a super retirement

**Women are more financially independent than ever but as they retire they are still at a significant financial disadvantage to men. Not only do women live longer, but they often face life cycle and financial hurdles that most men do not.**

A baby girl born in Australia today can expect to live to 84 while a baby boy can expect to live to 79<sup>1</sup>. While this is good news, it does pose specific challenges for women. Not only do they need to make their savings stretch further in retirement than men of the same generation, but they typically have less money to show for their life's work.

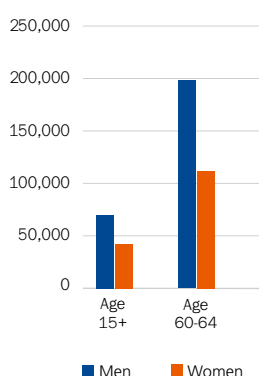
### Challenges:

- Women are the often sole caregiver, especially after divorce, leading to an increase in short-term costs.
- Broken periods of work lead to lower income.
- Women live longer and therefore need more funds after retirement.

### The gender money gap

After 20 years of compulsory superannuation, women still retire with little more than half as much in the kitty as men. In 2009/10, the average retirement payout was close to \$198,000 for men but only \$112,600 for women.<sup>2</sup> As these are averages, many women retired with much less. Worse still, 38.5 per cent of women had no super at all.<sup>3</sup>

### Average superannuation balances (\$) 2009-2010



Source: Association of Superannuation Funds of Australia

When you compare these final super payouts to the cost of living in retirement, it is clear they don't add up. According to the Association of Superannuation Funds of Australia, a married couple needs \$55,080 a year to meet their definition of a 'comfortable' lifestyle in retirement, while a single woman needs \$40,297 a year.<sup>4</sup>

No doubt balances will grow as the superannuation system matures and the Superannuation Guarantee paid by employers to their employees increases from



9 per cent to 12 per cent by 2019. But that is a long way off and it will not be enough to provide a financially secure retirement for older women who have not received the full benefits of compulsory super or those with extended periods out of the workforce.

### Long-term thinking begins at 40

Retirement tends to be out of sight and out of mind for younger women, but that begins to change some time after their 40th birthday. Suddenly retirement is within sight but many women realise they are financially lagging behind their male peers. This can happen for a variety of reasons:

- Women are more likely to take time out of the paid workforce to care for young children. When they do return to work, it is often part-time, possibly for some years.
- Even when women do return to work full-time, they are likely to be paid less than their male counterparts. As at November 2011, women earned 17.6 per cent less than men, averaged out across all industry sectors.<sup>5</sup>
- Divorce or widowhood often means a financial setback for women.

As a result of these circumstances, women tend to be more focused on the daily challenges of juggling work and family and often struggle to find the time and surplus cash to invest in their own future. Any savings they do put aside are likely to be earmarked for the mortgage and debt reduction or short-term goals such as a holiday, leaving an important long-term goal like retirement as a lower priority.

### A super plan

With careful planning and the help of your financial adviser, there are some simple strategies you can put in place that will make

a real difference to your future financial security, without sacrificing today's lifestyle:

- The most painless way to contribute more to super is to speak to your employer about salary sacrifice. A small amount taken out of your pre-tax salary on a regular basis will not only boost your retirement savings but will also reduce the amount of tax you pay.
- You can also make voluntary contributions from your after-tax pay up to a maximum of \$25,000 a year. And if you are eligible for the super co-contribution the government will match your contribution up to a maximum of \$500 a year.
- If you have a higher-earning partner, he or she may be able to make contributions to your super under the spouse contributions offset.

Talk with your adviser about your options and check the ATO website, [www.ato.gov.au](http://www.ato.gov.au).

Whatever strategy you follow, the sooner you get started, the longer your money has to grow, and the more you have to look forward to in retirement.

- 1 <http://www.abs.gov.au/ausstats/abs@.nsf/Lookup/by+subject/4125.0~Jan+2012~Main+Features~Life+expectancy~3110>
- 2 <http://www.superannuation.asn.au/ArticleDocuments/116/rc1109-LevelAndDistributionOfRetirementSavings.pdf.aspx>
- 3 ASFA Superannuation Statistics <http://www.superannuation.asn.au/resources/superannuation-statistics/>
- 4 ASFA Retirement Standard, [http://www.superannuation.asn.au/ArticleDocuments/129/ASFA\\_RS\\_Budgets\\_March2012.pdf.aspx](http://www.superannuation.asn.au/ArticleDocuments/129/ASFA_RS_Budgets_March2012.pdf.aspx)
- 5 Equal Opportunity for Women in the Workplace [http://www.eowa.gov.au/Information\\_Centres/Resource\\_Centre/Statistics/Statistics\\_Archive/Gender\\_Pay\\_Gap\\_Fact\\_Sheet\\_Feb2012\\_PDF.pdf](http://www.eowa.gov.au/Information_Centres/Resource_Centre/Statistics/Statistics_Archive/Gender_Pay_Gap_Fact_Sheet_Feb2012_PDF.pdf)



# Where's the big idea?

As citizens of a young nation living on the world's oldest continent, Australians have always been challenged to think big and make this thinking a reality.

Think of the Snowy River Scheme – 21 years to build at a cost of \$5 billion in today's dollars<sup>1</sup> or the Sydney Harbour Bridge, planned as the world's longest single span bridge – 10 years to design and build at a total cost of around \$143 million in today's dollars.<sup>2</sup> And then think where Australia would be today without the electricity generated by the Snowy Scheme? Or a road and rail bridge which allows many thousands of people to cross Sydney harbour in just minutes?

Sadly, one of the many unfortunate side effects of the global crisis and the continuing issues in Europe seems to have been the crushing of our desire to make big plans and achieve them.

## What matters to Australians today?

What Matters to Australians, a research report released in May 2012, tells us how our priorities have changed under the pressures of recent global financial turmoil. The report captures our responses to the financial concerns that emerged in 2007, showing how they have cramped our style and narrowed our outlook.

In 2007, Australians named big picture issues like environmental sustainability and global security as the most important to them. Today, however, the issues that matter most to us are food and health, local crime and safety, and basic services, all quite personal concerns.<sup>3</sup>

It seems that our thinking is now based on day-to-day survival rather than concern for the future of the world we live in. This is not because food quality, safety and basic services for ourselves and our families were regarded as unimportant in 2007, but that five years ago we used to give priority to wider issues as well.

Financial advisers are aware that this trend also affects how investors think and make decisions. Traditionally the role of advisers has been to help clients achieve financial security and the satisfaction that can be achieved through long term planning. In other words, financial advice is about helping individuals to clearly define their goals and reach them; it is not confined to helping clients simply toward financial survival, even in a crisis.

## Letting the GFC put your future on hold?

Nothing lasts forever, including the financial problems of the euro zone. In fact, taking a long-term view, this is a good time to start thinking beyond the current financial crisis to re-evaluate and redefine your broader financial goals.



One good reason for re-evaluating your investment strategy is that even after the good times return, things won't be the same as they were, and pre-2007 strategies may no longer be appropriate.

For a start, you will be at least five years older, your risk profile may have changed, your career path might have taken a new turn, and your family circumstances and personal ambitions might be quite different.

## The risks of short-term thinking

One common reaction from investors has been to shift a significant proportion of their assets into cash or term deposits. While this is an understandable response, it is unlikely to be a long-term benefit for most investors. The main risk of such a defensive investment is that it fails to protect your capital against the erosion caused by inflation.

The table shows different rates of inflation and how it impacts the value of your capital over time. Fixed interest returns are limited to the extent they don't offer capital growth (only interest payments) as a natural offset against the effects of inflation.

Inflation rate* (per cent)	Value of \$1000 over 10 years	Value of \$1000 over 15 years	Value of \$1000 over 20 years
1.6	853.22	785.10	724.27
2.6	773.62	673.57	590.44
3.6	693.06	576.97	480.33
4.6	624.43	493.43	389.91

\* The annual Australian inflation rate varied between a low of 1.58 and a high of 5.99 per cent between 1992 and 2012

## Thinking bigger, aiming further

Just as it is important with your money, thinking long-term and drawing on inspiration and endeavour are also important for a community and a nation. As Franklin Roosevelt said, 'To reach a port we must sail – sail, not drift.'

As we know from current debates on topics as diverse as managing climate change, building an inland rail line or faster internet, big ideas are difficult to define and often controversial in their implementation. History shows us, however, that big ideas are important for the human spirit, for setting national goals, and for leaving a valuable legacy to the generations that follow.

Whether we are a country, a family or an individual, we thrive when we have goals that extend beyond the day-to-day – and a plan which helps us bring them to reality.

1 <http://www.amazingaustralia.com.au/achievements.htm>

2 <http://www.genesis.net.au/~ejs/sydney/index.html>

3 'What matters to Australians: Our Social, Political and Economic Values', May 2012

4 <http://www.rateinflation.com/inflation-rate/australia-historical-inflation-rate.php?form=ausir>