



Institute of Actuaries of Australia

# 4th Financial Services Forum

*Innovation in Financial Markets*

19 and 20 May 2008 – Melbourne

## Presentation to Institute of Actuaries Australia, Financial Services Forum

### Industry funds versus retail funds - a retail perspective

Nicolette Rubinsztein - General Manager, Strategy

Peer review: Peter Labrie, Head of Super & Investment Services

Colonial First State

May 2008

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# Outline

- The backdrop
- FirstChoice – a case study
- Investment performance
- Fees
- What else?
- Conclusion



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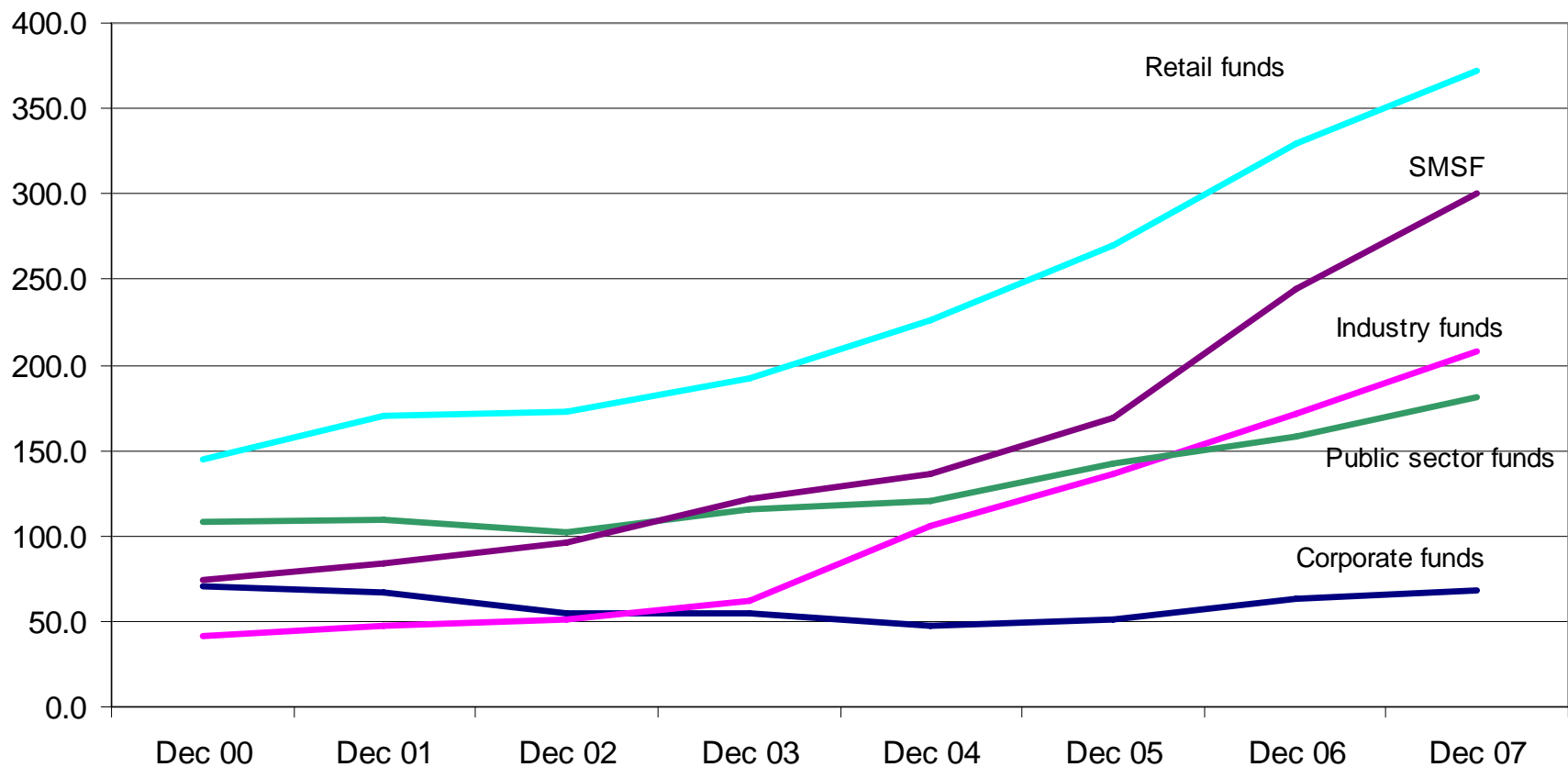
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# Superannuation fund assets

Retail is largest sector, followed by SMSFs then industry funds







# APRA data

Appears that industry funds have outperformed retail funds

**Table 8: Ten-year average return on assets and volatility**

Entities with at least \$100 million in assets

	June 1997	June 1998	June 1999	June 2000	June 2001	June 2002	June 2003	June 2004	June 2005	June 2006	1997-2006	
											Average return	Volatility
All entities	12.5%	6.8%	6.8%	9.7%	3.0%	-5.0%	-2.1%	11.2%	11.5%	12.4%	6.7%	6.2%
Corporate	14.9%	8.5%	8.6%	11.0%	4.7%	-3.9%	-3.1%	11.4%	12.6%	13.5%	7.8%	6.6%
Industry	11.7%	6.6%	6.5%	9.0%	3.2%	-5.0%	-1.8%	12.4%	12.1%	12.6%	6.7%	6.2%
Public sector	16.3%	6.9%	8.3%	12.3%	3.1%	-6.0%	-0.9%	12.6%	13.2%	13.9%	8.0%	7.2%
Retail (excluding ERFs)	8.0%	5.8%	4.8%	7.7%	2.2%	-5.0%	-2.7%	10.1%	10.3%	11.4%	5.3%	5.5%
ERFs	7.3%	7.3%	4.1%	6.6%	3.6%	2.4%	3.6%	5.6%	6.3%	7.0%	5.4%	1.8%



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## The headlines



### THE AUSTRALIAN

Australia's national daily newspaper

Finance

Industry funds still have the edge over their retail rivals

### The Sun-Herald

Investor  
Industry funds lead the way

#### GOOD REASON TO GO NOT-FOR-PROFIT

Publication: AFR Summary , Page 54 (Mon 13 Aug 2007)

Author: Barrie Dunstan

The Sydney Morning Herald

Money  
Industry funds dominate field

THE AUSTRALIAN

#### RETAIL SUPER FUNDS UNDERPERFORM ALL THE REST IN PAST DECADE: APRA

Publication: The Australian , Page 019 (Fri 27 Jul 2007)

Author: Anna Fenech

Business News  
Industry funds outdo others



### The Courier-Mail

News  
Industry funds 'yield far more'

The Sydney Morning Herald

#### SUPER BOOMING, BUT NOT ALL FUNDS SEE HAPPY RETURNS

Publication: Sydney Morning Herald , Page 18 (Fri 27 Jul 2007)

Author: Jacob Sautwick

### THE Daily Telegraph

Money coach  
Finance  
Industry funds thrash overpriced rivals

### The West Australian

#### RETAIL SUPER FUNDS FARE POORLY IN 10-YEAR SURVEY

Publication: The West Australian , Page 12 (Fri 27 Jul 2007)

Author: SHANE WRIGHT

Herald Sun

BUSINESS  
Industry super on top

#### Super fund returns compared

"Why don't financial planners recommend industry funds? It's because we don't pay commission."



Figures from the Australian Prudential and Regulatory Authority (APRA, see above) show the average annual returns for the five main types of super fund over 10 years from June 1996 to June 2006. It's notable that retail funds, open to any investor, were the worst-performing, at 5.3% pa. They were even slightly worse than eligible rollover funds, which hold lost and unclaimed super.





# Net superannuation switches

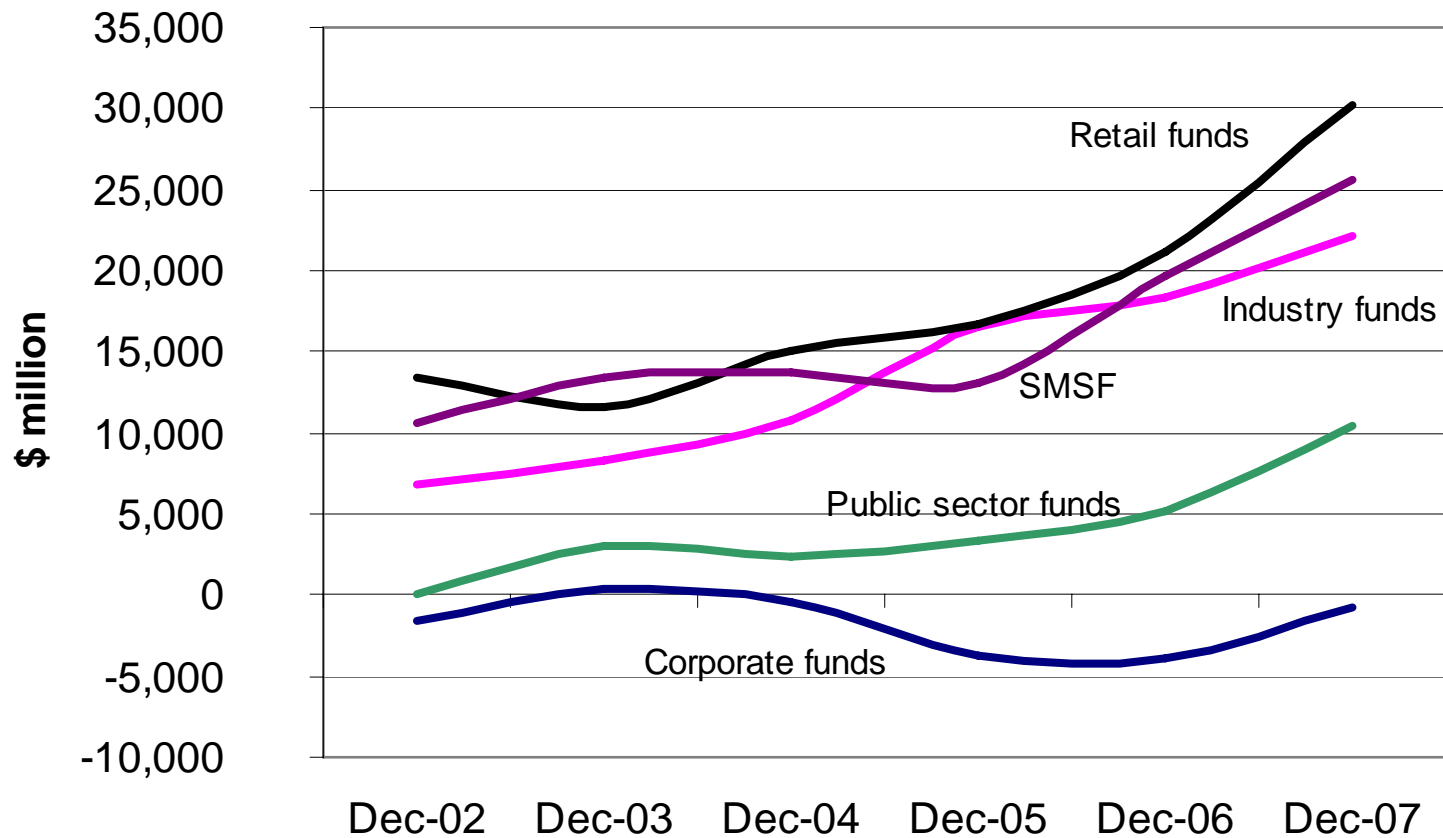
Results for number of switches is a mixed bag

Superannuation Fund Managers	12 Months to September 2007		
	% of Switched Products Gained	% of Switched Products Lost	Net Share of Switched Products
Commonwealth Group	7.8	6.7	1.1
Suncorp Group	2.2	1.1	1.1
St George Group	3.4	2.8	0.6
AXA Group	2.2	2.1	0.1
National Group	5.0	5.3	-0.3
ING Group (inc. ANZ JV)	4.1	4.6	-0.5
Industry Funds	35.6	37.0	-1.3
Westpac Group	2.8	4.2	-1.4
AMP Group	6.9	10.2	-3.3
Public Sector Funds	9.1	5.3	3.8
Self managed funds	3.4	1.1	2.4
Other	17.5	19.7	-2.2
<b>TOTAL</b>	<b>100.0</b>	<b>100.0</b>	<b>0.0</b>



# Superannuation fund net flows

Net flows highest for retail, followed closely by SMSFs and industry funds



Source: APRA net contribution flows – Quarterly Superannuation Performance Statistics, ATO. Netflows are annual from Jan through end Dec each year, except SMSF data for 04 through 07 which is annual from July through June.



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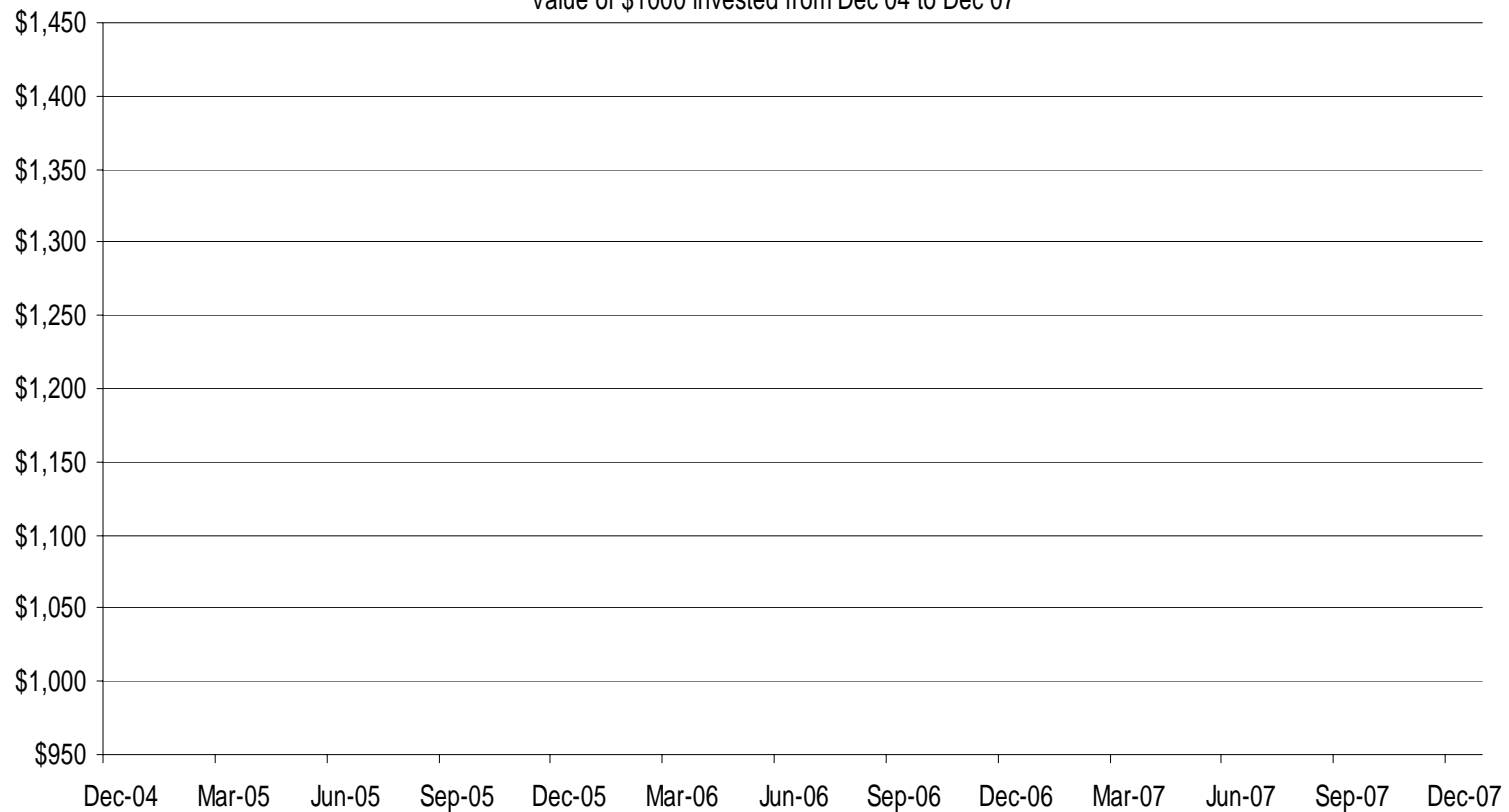
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# Investment performance

FirstChoice performance compares favourably to industry fund average

Value of \$1000 invested from Dec 04 to Dec 07

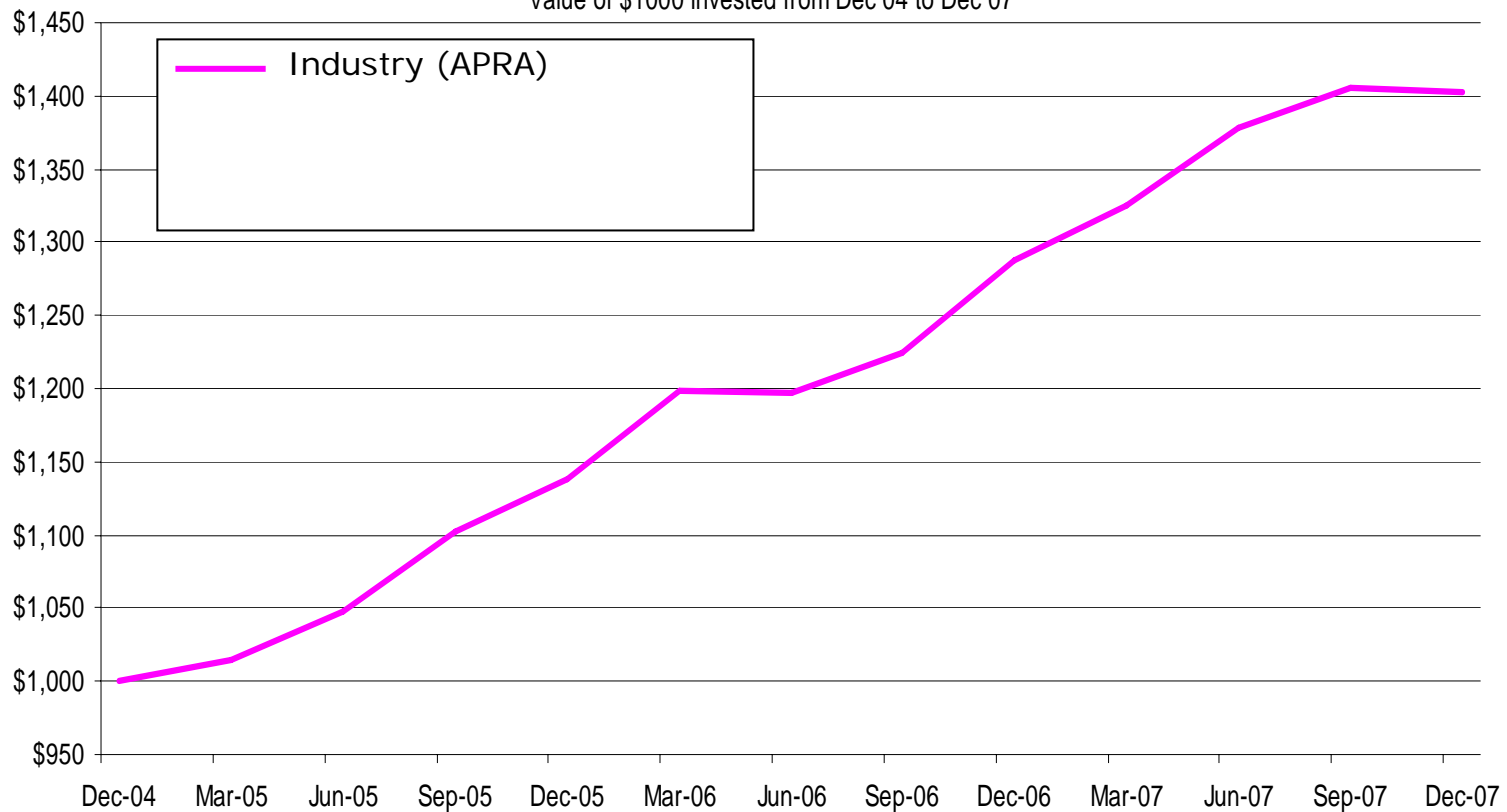




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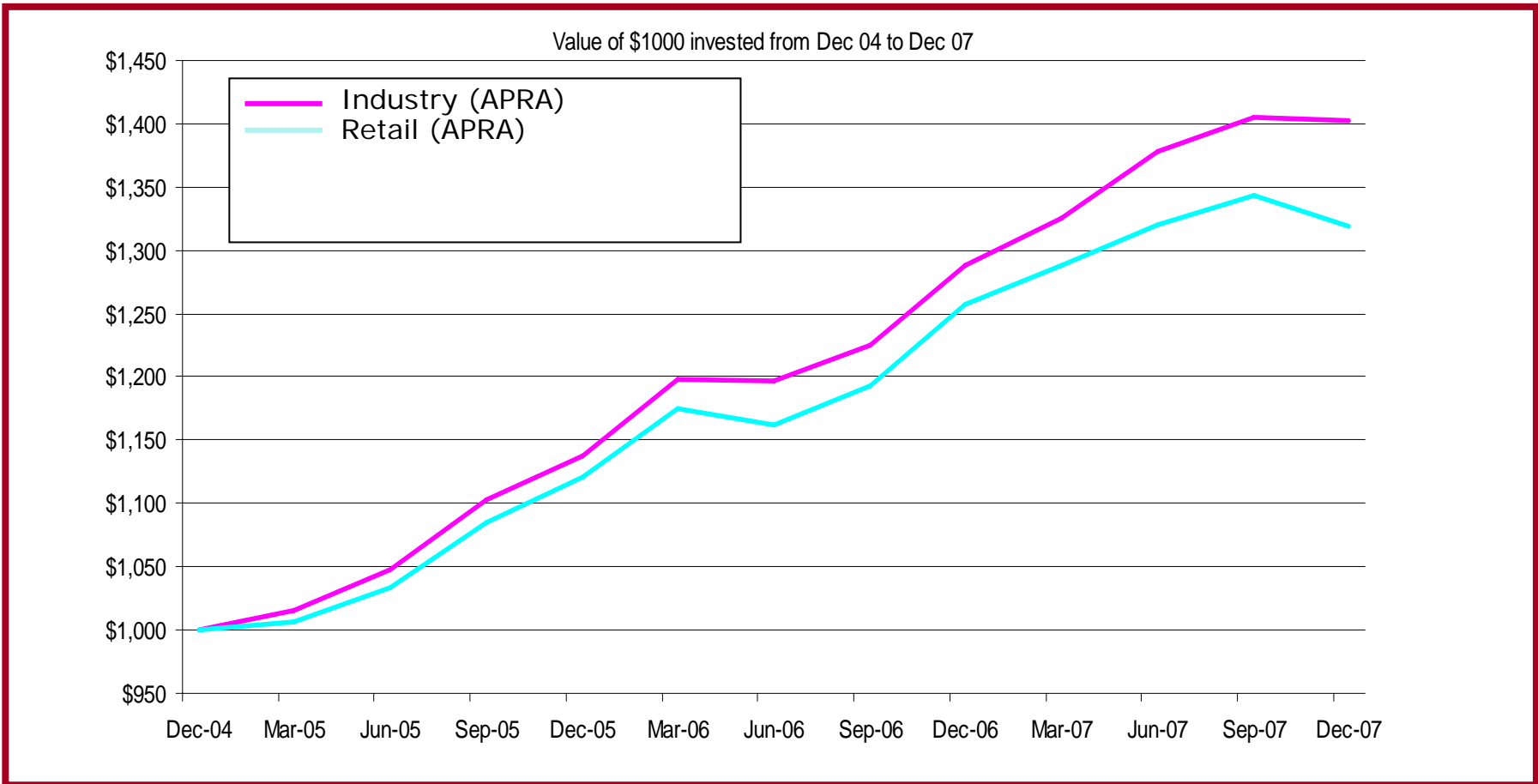
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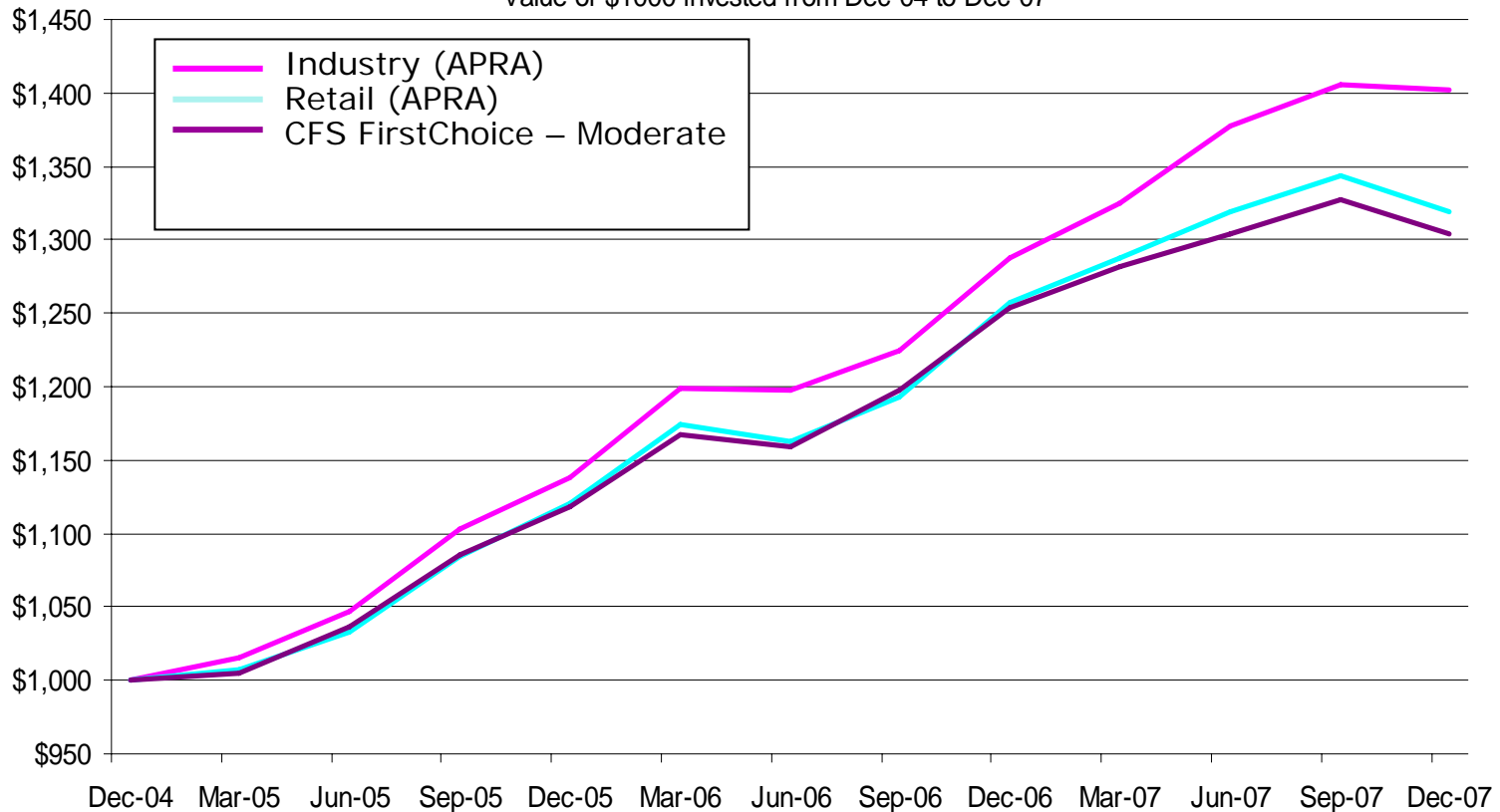




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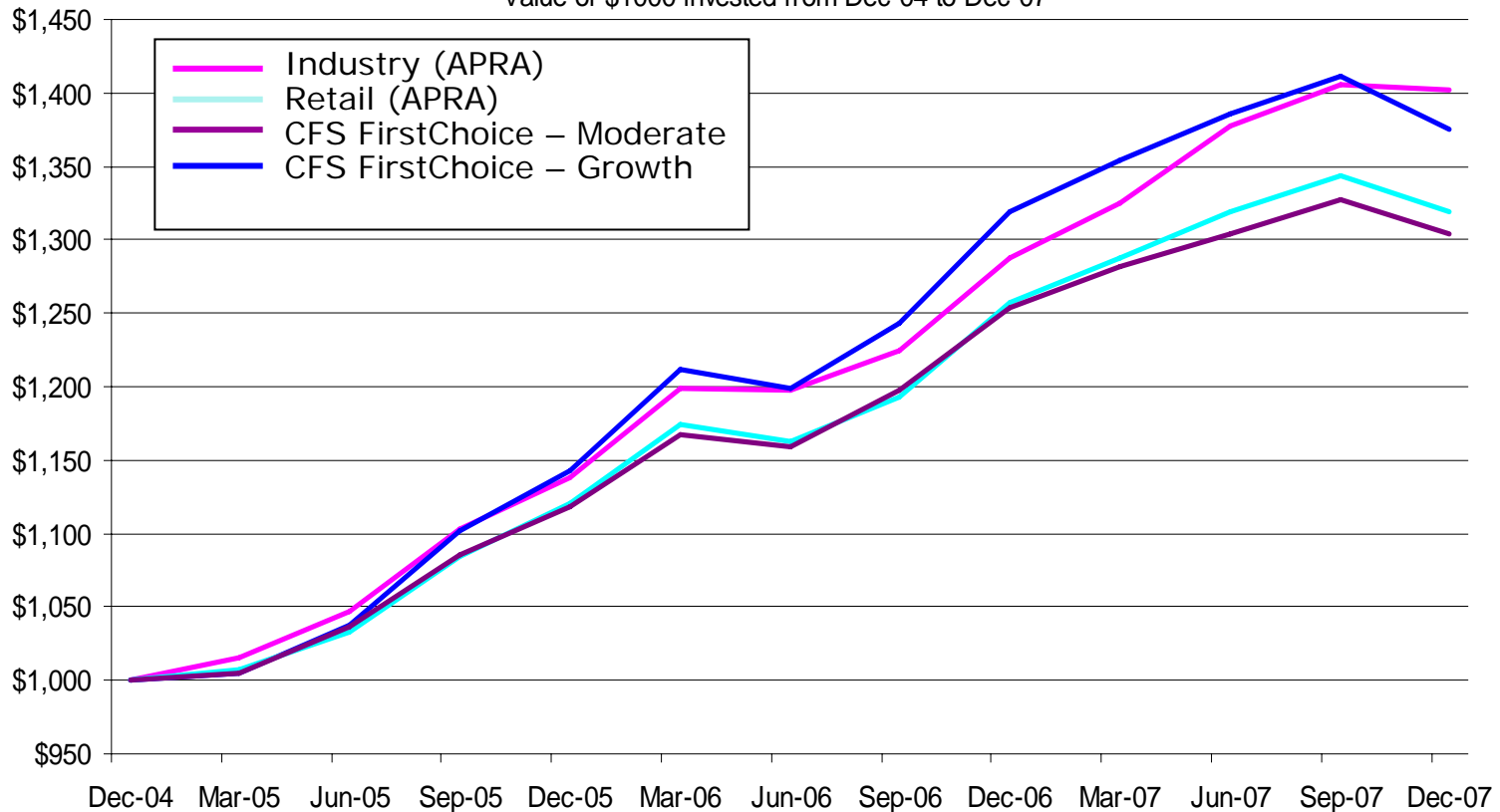




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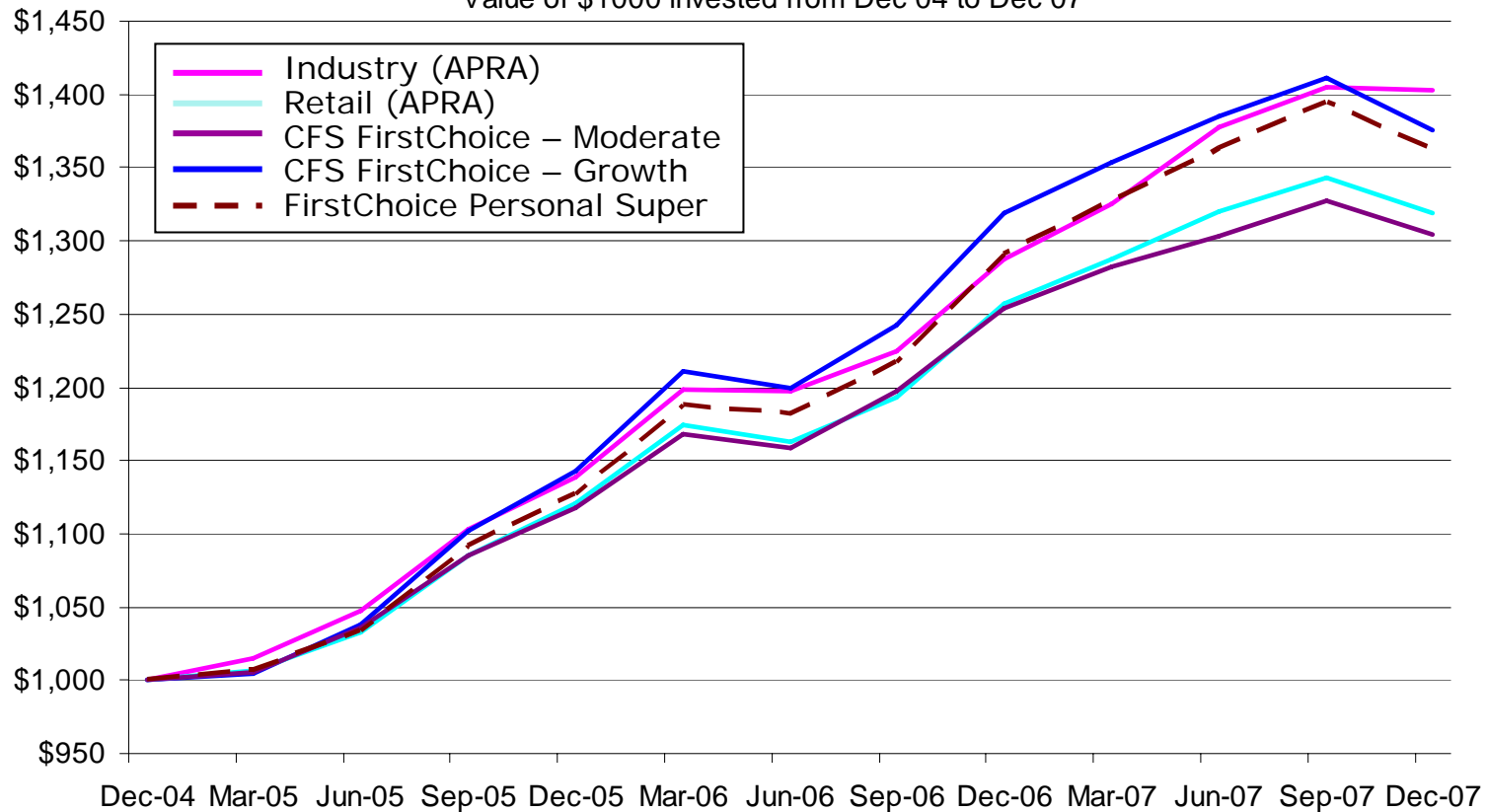




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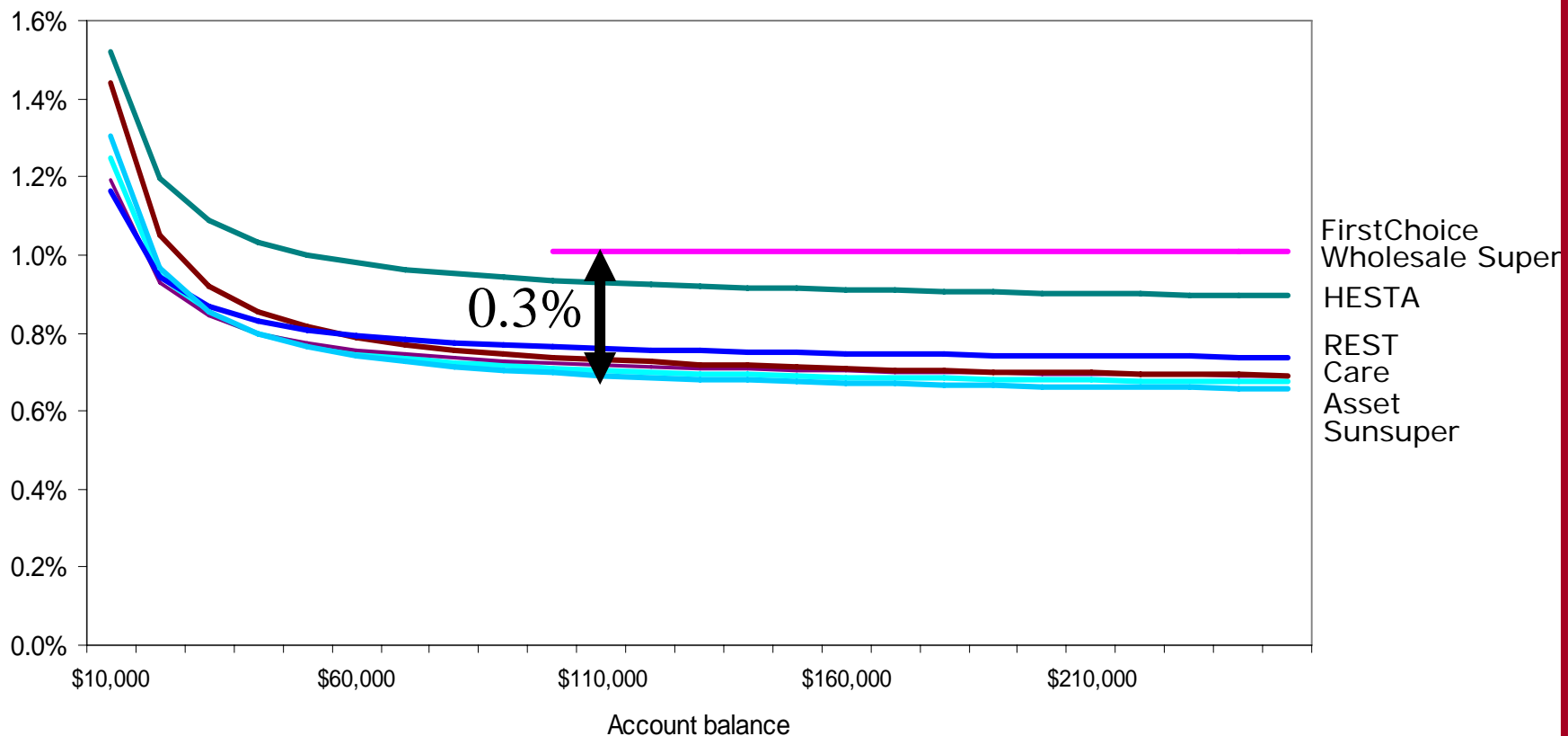
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# Fees

FirstChoice Wholesale fees are 6-35bps higher than key industry funds





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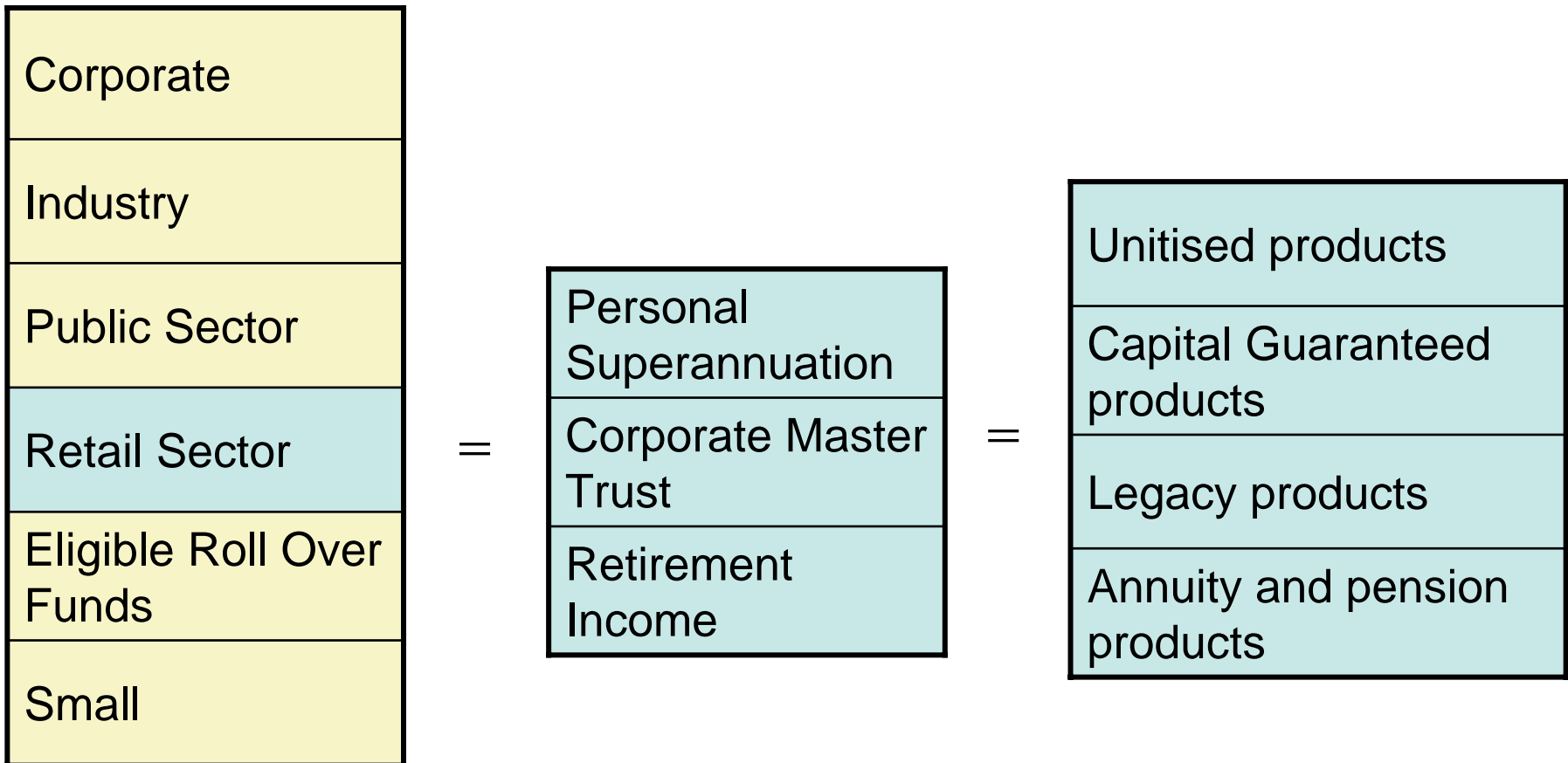
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Industry	11.7%	6.6%	6.5%	9.0%	3.2%	-5.0%	-1.8%	12.4%	12.1%	12.6%	6.7%	6.2%
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# Composition of retail sector

APRA categorisation – retail sector is diverse





## Why do retail funds appear to under-perform?

It is mainly due to the strategic asset allocation and fees

- The default fund has much less emphasis in retail funds due to advice
- Retail fund asset allocations are the amalgamation of thousands of individual decisions
- Trying to compare the asset weighted returns in this environment is almost meaningless
- Retail clients are older
  - much higher numbers of pre-retirees and retirees
  - the older clients hold the bulk of the assets
- The SAA of retail funds is more conservative in aggregate



# Comparison of asset allocations

Retail funds have a lower allocation to growth assets on average

	June 2004 - June 2006 (3 year average)	
	Growth	Other
Corporate	69%	9%
Industry	69%	10%
Public Sector	70%	7%
Retail	53%	18%



## Impact of asset allocation on performance

A 20% difference in allocation to growth assets made a 1.2% p.a performance difference over this period

	High Growth Funds (81-100%)	Growth Funds (61-80%)	Difference
3 years to 31 Dec 2007	13.3%	12.1%	1.2%





# Impact of fees

Industry fund fees are lower than retail funds by approximately 0.75%

		<b>Expense Rate 2006 %</b>
Wholesale	Corporate	0.78
	Public Sector	0.70
	Industry	1.13
	Corporate Master Trust (lge)	0.81 (0.02)
Retail	Corporate Master Trust (sml)	2.01 (0.46)
	Personal Super	2.12 (0.55)
	Retirement Income	1.79 (0.53)
Small	SMSFs	0.87 (0.15)

0.75% difference (includes 0.5% advice)

Retail weighted average is 1.88% (includes 0.5% advice)



# Comparing like with like

Performance has been similar except 2002 and 2007

Net of tax and investment fees - % annual performance to 31 Dec for "Growth Funds" (61% to 80% growth assets)

	2007	2006	2005	2004	2003	2002	2001	2000
Industry Funds	9.3	14.1	14.4	15.1	9.9	-3.0	5.4	8.4
Master Trusts	6.4	14.4	14.6	15.8	8.6	-6.4	4.1	7.5



Global shares was worst performing asset class in last 10 years  
 (especially 2002, 2007)

Sector Names	Australian shares	Global shares	Australian Property Securities	Australian Fixed Interest	Cash
Year ended 31 December % return					
1998	8.5	32.0	18.0	9.5	5.1
1999	19.3	17.1	-5.0	-1.2	5.0
2000	6.3	2.2	17.9	12.1	6.3
2001	10.5	-9.7	14.6	5.5	5.2
2002	-8.6	-27.2	11.8	8.8	4.8
2003	15.0	-0.5	8.8	3.1	4.9
2004	27.9	10.3	32.0	7.0	5.6
2005	22.5	17.0	12.5	5.8	5.7
2006	24.5	11.7	34.0	3.1	6.0
2007	16.2	-2.1	-8.4	3.5	6.7
10 year return (annualised)	13.7	3.9	12.9	5.6	5.5

Source: S&P/ASX 300 Accumulation Index, (ASX All Ordinaries Accumulation Index pre April 2000), MSCI World Net Index (\$), MSCI World Net Index AUD Hedged, S&P/ASX 200 Property Accumulation Index (ASX Property Trusts Accumulation Index pre April 2000), UBS Australian Composite Bond Index 0+ Years, Citigroup World Government Bond Index ex Australia AUD Hedged, UBS Australia Bank Bill Index. **Past performance is no indication of future performance.**



The key drivers of performance differences were allocation to international equities, alternative assets and listed property

Differences in allocation - 2006

	Industry funds	Retail funds
International equities	24%	28%
Alternative assets	4%	11%
Property	11%	8%

“Consultants generally expect Australian and international shares to produce similar pre-tax long-term returns, and property to produce lower returns. This suggests that the out-performance of industry funds over the past six years **may not be sustainable**”.



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If you compare like with like and allow for advice, differences appear reasonable

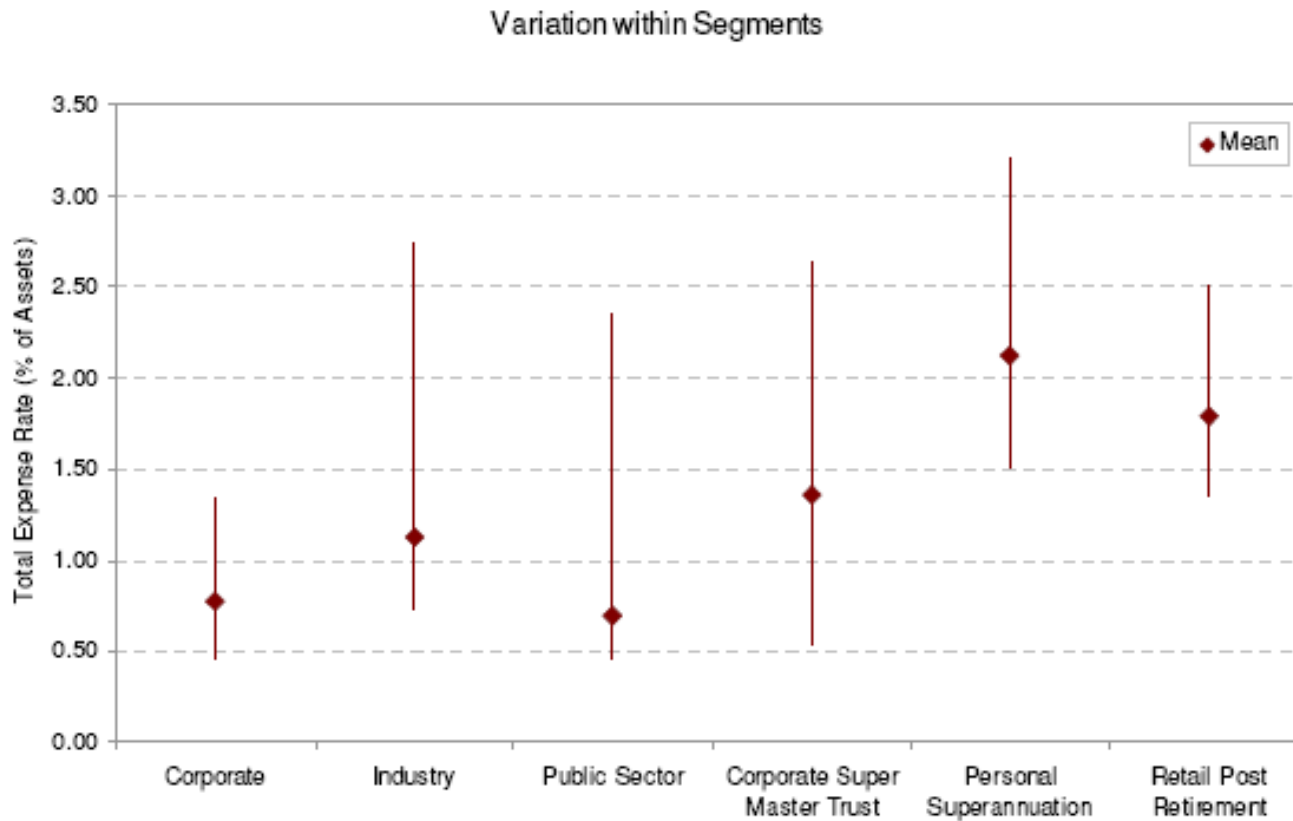
**Average Fee by Account Balance (% of Assets), excluding advice**

Sector	Segment	\$5,000	\$20,000	\$50,000
Wholesale	Corporate	1.71	0.97	0.82
	Corporate Super Master Trust	1.60	0.86	0.71
	Industry	2.05	1.10	0.91
	Public Sector	0.84	0.72	0.70
Retail	Corporate Super Master Trust	2.90	1.67	1.42
	Personal Superannuation	1.91	1.60	1.54
	Retirement Income	1.65	1.34	1.28
	Retirement Savings Accounts	2.30	2.30	2.30
	Eligible Rollover Funds	2.53	2.53	2.53



# Fee variability

There is a lot of variation – misleading to compare averages





# Issues with fee comparisons

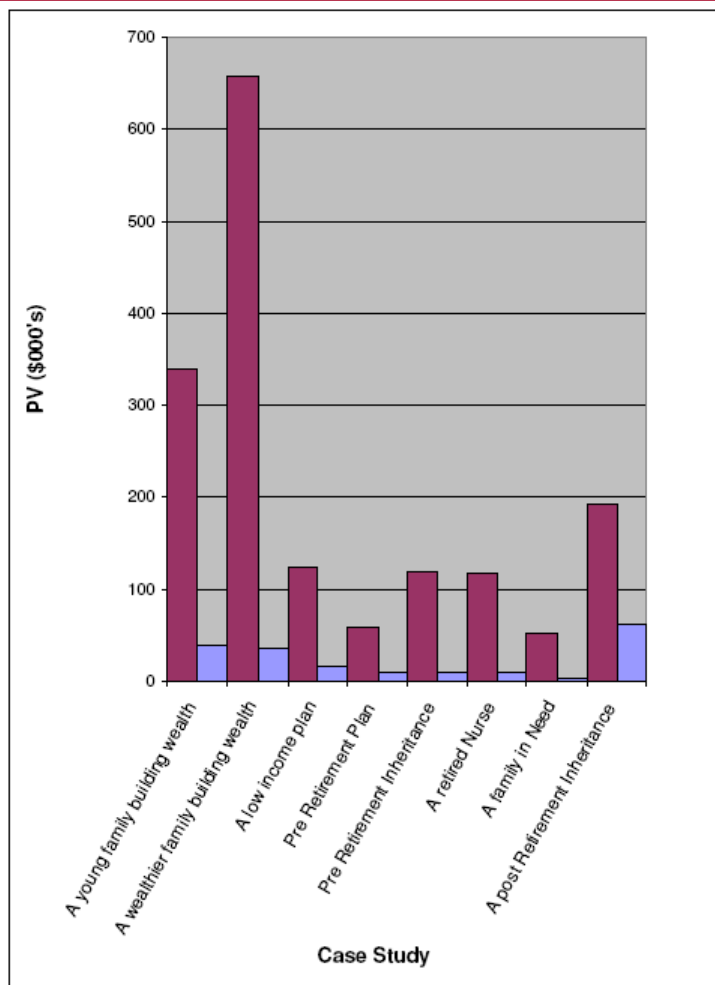
- No allowance for employer discounts (assumes small employer)
- Do not factor in value of advice
- Compares averages
  - not full universe
  - lots of variation
  - retirement products
- Assumes static fees





# The value of advice

Need to consider cost of advice relative to value of advice



■ Cost of Advice ■ Value of Advice



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## Why don't financial planners recommend industry funds?

It is not because they don't pay commissions



[ABC Online](#)

### **PM - Research questions objectivity of financial planners**

**PM - Tuesday, 17 July , 2007 18:46:00**

**Reporter: Stephen Long**

MARK BANNERMAN: Thousands of Australians have been piling money into superannuation to take advantage of tax changes announced in the Federal Budget, and before doing so, many turned to financial planners for advice.

But how objective is the advice they're giving?

New research says that of the top 30 financial planning advisory groups, not one has an industry super fund on their approved list of schemes to recommend.

Yet many industry funds are high-performing and typically charge lower fees than private sector retail funds.

**The Industry Super Funds say advice to consumers is being corrupted by the commissions paid to financial planners.**

**Note: Over 100% of Colonial First State's retail net flows are into products that don't have in-built commissions**



# Where are the gaps?

What do dealer groups and advisers look for?

- Business strength (operational risk)
- Number of investment options
- Daily unit pricing
- Insurance premiums based on gender, age, occupation
- Insurance cover – death, TPD, salary continuance, AAL's
- Functionality to match planning strategies (eg binding death benefits)
- Reporting timeframes
- T+1 transactions (transaction speed)
- Online transactions
- Adviser remuneration flexibility
- Performance data to research houses
- B2B infrastructure
  - Online adviser tools
  - Online adviser reporting
  - Datafeeds to financial planning software
- Funds rated by research houses

} Reduces  
the cost  
of advice



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Account value (\$): From/To [ ] to [ ] e.g. 5000.00

All margin lending clients

Margin loan balance (\$): From/To [ ] to [ ] e.g. -50000.00

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Client's age: From/To [ ] to [ ]

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**Retrieve reports**

Download reports you have submitted or view scheduled reports.

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The following table contains the status of the reports you have requested. Refresh to update the status.

Filter by report type: All Refresh

Report name	Report timeframe	Created	Format	File size	Status
FUA by client	17/04/2008	PDF	-	-	Pending
Client Listing	08/04/2008	CSV	-	-	<a href="#">Download</a>
Investor Summary	08/04/2008	CSV	-	-	<a href="#">Download</a>
Client Review Report	04/04/2008	ZIP	0.4Mb	-	<a href="#">Download</a>
Client Review Report	04/04/2008	ZIP	0.55Mb	-	<a href="#">Download</a>
Transaction Summary	01/04/2008	CSV	-	-	<a href="#">Download</a>
FUA by client	28/03/2008	PDF	0.01Mb	-	<a href="#">View</a>
Client Review Report	28/03/2008	ZIP	0.09Mb	-	<a href="#">Download</a>
Transaction Summary	11/03/2008	CSV	-	-	<a href="#">Download</a>
Transaction Summary	19/02/2008	CSV	-	-	<a href="#">Download</a>
Transaction Summary	05/02/2008	CSV	-	-	<a href="#">Download</a>
Client Review Report	21/06/2006	ZIP	-	-	Failed

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Schedule name	Reporting period	Report frequency	Next report
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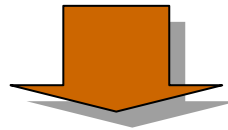
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# Conclusion

- Performance differences are due to:
  - lower allocation to growth assets for retail funds on average
  - fees (mainly advice)
  - unusual period for international equities in last 10 years
- Fee differences
  - reasonable quantum, when compare like for like
  - biggest variation is cost of advice – compare to value of advice
  - long list of additional product features and services



- Need to look behind the numbers!
- Who will win?
  - no one particular sector – the good funds within each one