

Superannuation Performance Test Regulations 2023

May 2023

Introduction

Frontier Advisors is pleased to provide this submission to Treasury's consultation on the Your Future, Your Super (YFYS) performance test regulations.

Frontier is one of Australia's leading institutional investment advisers. We have been advising Australian institutional investors as a trusted adviser for over twenty-five years. We provide advice on more than \$600 billion of assets across the superannuation, charity, public sector, insurance and higher education sectors. The fact our advice is free of any product, manager or broker conflicts, means we can provide truly unconflicted advice aligned with our client's best interests.

As an asset consultant, our submission concentrates on the performance test.

As we have mentioned in our previous submissions, Frontier supports a well-designed performance test. We view the proposed changes to incrementally improve the performance test.

However, continue to have concerns with the current performance test, as detailed in our previous submissions. We recommend there be a further and more detailed review of the YFYS performance test over the next year to ensure the test promotes members best financial interests. This should be completed, including regulatory changes by the first quarter of 2024.

Feedback on specific changes

Frontier supports extending the lookback period for performance testing from 8 to 10 years as data for longer period become available to encourage longer-term investment decisions.

In respect of the proposed benchmarks, we provide the following feedback:

Asset class	Frontier feedback
International equity (developed and emerging markets)	<p>We welcome the new developed/emerging markets split however question the use of custom tax series. In addition, the emerging market fee is inconsistent with passive management products.</p> <p><i>Change to standard indices. Increase fee adjustment for emerging markets.</i></p>
International unlisted property	<p>Uninvestable benchmark. A new benchmark which is unrepresentative of fund allocations. Unfrozen so results may change historically. Not a freely available benchmark and expensive to buy.</p> <p><i>Maintain current (Australian) index until an appropriate and robust international index is developed.</i></p>
Unlisted infrastructure	<p>Moving from weighted average to median causes more complications in data integrity – every time a fund is added/removed from the Unfrozen index is likely to result in the whole time series changing. The median is a compounded quarterly result as such uninvestable. Frontier has extensive experience in infrastructure indices and would be happy to participate in a technical group.</p>

Asset class	Frontier feedback
	<i>Maintain current index until an agreed calculation method is developed.</i>
Australian fixed interest	<p>The proposed benchmark is rarely used by funds and is more complex (more index constituents, additional market segments including inflation linked bonds and floating rate debt securities). While the overall return profile is similar, we do not believe this change is additive to the test.</p> <p><i>Retain the Bloomberg Ausbond Composite 0+ index.</i></p>
Australian credit	Acceptable, but doesn't allow for low duration investments, which is more an issue for lower risk Trustee Directed conservative options.
International fixed income excluding credit	Acceptable.
International credit	<p>Superannuation funds' practice in this asset class varies from investing in investment grade credit, high yield securities, loans or emerging market debt, reflecting a range of credit risks and duration exposures. The choice of the high yield (non-investment grade) benchmark is not consistent with many of these exposures and this choice of a higher risk benchmark may influence funds to take more risk in this asset class. The proposed benchmark selection is also inconsistent with the approach for Australian credit exposures.</p> <p><i>Use the Bloomberg Global Aggregate Corporate Index (hedged AUD).</i></p>
Growth and defensive alternatives	Acceptable, although guidance on the types of strategies that are consistent with defensive or growth classifications will be useful.

The introduction of the YFYS performance test, particularly with the new indices, imposes a high explicit cost to each fund for the purchase of these benchmarks. In respect of the custom tax indices, we agree these are more appropriate but are not commonly used and produce only marginally different returns to the standard, more freely available indices.

As set out in the table above, we recommend the test use the standard, net dividends, indices for all equity asset classes. Alternatively, we recommend Treasury initiate a process for commercially provided indices to be made available to super funds on a collective and cost-effective basis.