Media Report

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Share boom delivers 12pc super return

Alison Kahler and Chris Wright

Superannuation funds are expected to achieve returns of 12.2 per cent in the year to June 30, fuelled by record highs on the stockmarket. This second consecutive year of double-digit returns comes as 4.8 million workers consider whether to switch to a new retirement fund.

The solid performance was achieved as the Australian sharemarket continued to outstrip many of the world's largest equity markets, with booming commodity prices driven by demand from China pushing the benchmark S&P/ASX200 Index to a record 4312.2 on June 17.

The sharemarket has risen by 19.8 per cent this financial year but fund managers have cautioned that the economy and company profits are slowing, dampening hopes of another bumper return for super funds next year.

Estimates from independent analyst SuperRatings suggest that the best balanced super fund – the investment option chosen by more than 80 per cent of Australians – will return 12.9 per cent in the year to June 30. Even the worst funds are expected to gain 11.4 per cent.

The strong performance of the past two years – super funds returned a median 13.3 per cent in the 2003-04 financial year – means that $10,000 invested in the average fund five years ago is now worth $13,021 after fees and tax.

MONEY MATTERS

"Following the introduction of choice, superannuation will be a critical element of enterprise bargaining"
– David Whiteley, ACTU, page 8.

Investment bankers hit by sharp fall in mergers, **page 51.**

Macquarie Bank does it again, Chanticleer, **back page.**

The big gains will renew investor confidence in super three days before the introduction of super choice laws that will allow many workers to switch out of their employer's retirement fund for the first time.

The top funds for 2004-05 are likely to include the $8.2 billion Retail Employees Superannuation Trust, Queensland public sector fund QSuper and the $5 billion Health Super scheme, SuperRatings says.

"Our returns were very much driven by the performance of our fund managers," REST chief executive Neil Cochrane said. "The

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advice from our asset consultant has been to use boutique managers both locally and offshore – and it has paid off. We use 26 fund managers, including Paradice Cooper Investors, 425 Capital and Orion Asset Management.

"But expectations of another 12 per cent return next year are overly hopeful. We've had two very good years and must expect things will cool down. It will suit us because we have a defensive position, a higher allocation to cash and fixed interest than the average manager," Mr Cochrane said.

SuperRatings estimate of the median return is based on actual returns to May 31, the performance of financial markets so far in June and the average asset allocation of balanced super funds.

The chief investment officer of the $15 billion UniSuper fund, David St. John, said its returns were sustainable because of its sheer size.

"Our returns [over the past year] were derived from Australian shares, international shares and alternative assets in roughly equal proportions. Key contributors include Ausbil Dexia in Australian shares and Bernstein, Fidelity Investments and Mondrian Investment Partners in international equities. We also had a tilt to emerging markets," he said.

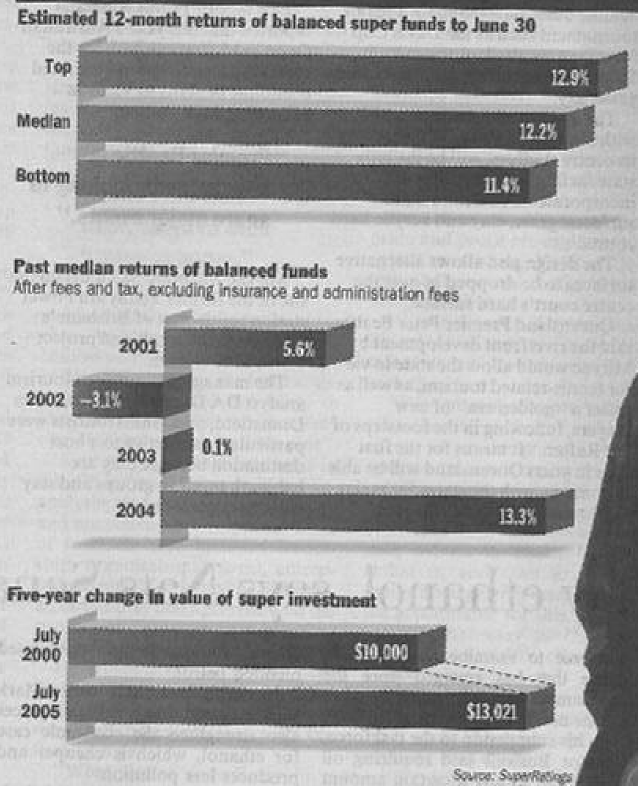
"Our returns are sustainable because of our size – we have an unconstrained investment universe. Our size also means we can keep operating costs very low."

The fees paid by super members have been a controversial issue in the lead-up to super choice, sparking heated debate in different sectors of the industry.

The chief executive of the $6.5 billion First State Super scheme, Michael Dwyer, said its fees helped it maintain solid returns for investors, and claimed members paid only 0.28 percentage points for investment management in the 2003-2004 financial year and another $52 for administration.

"About 50 per cent of all our money is in indexed funds. When the markets go well, you get the benefit of index returns and low costs," Mr Dwyer said.

THAT'S SUPER



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– Neil Cochrane, Retail Employees Superannuation Trust chief executive

But the old-fashioned pricing mechanisms of some super funds are proving controversial. Pressure is growing for not-for-profit industry funds to switch to the more modern method used by commercial financial institutions, a move that could cost millions of dollars and considerable resources.

Almost all retail funds use a system called forward pricing, where applications to buy and sell units are processed using a price calculated after those applications have been received, and usually on a daily basis.

But most industry funds use a different method called a crediting rate. This can be calculated weekly, monthly, quarterly or even annually, and is widely seen as less precise than unit pricing.

Crediting rates will come into the spotlight with choice of super as many industry funds, previously only open to selected professionals, become public offer to capitalise on the new laws. The market timing and late trading practices that were the subject of great scandal in the US last year, in which investors took advantage of changes in asset valuations not yet reflected in fund unit prices, are much easier to carry out in a crediting rate system than in unit pricing.

"If you are doing historical pricing, you really are open to manipulation, particularly if you are public offer and trying to attract a broader client base," Intech Investment Consultants executive director Brett Elvish said.

Unit pricing was the subject of an Australian Securities and Investments Commission and Australian Prudential Regulation Authority consultation paper in December last year, the results of which are expected in the third quarter.

Several groups are known to have written to the regulators suggesting that all funds should use unit pricing methods. One, management consultant Deloitte, wrote: "It is suggested that ASIC and APRA introduce regulatory policy that all new funds . . . calculate unit prices using only forward pricing."

The results of the consultation paper will not force industry funds to make the shift: it will be a set of guidelines, not legislation. But some, such as FuturePlus which represents the local government and energy industries, have already done so.

"I suppose they could require it, but the issue is going to be with funds like us with a lot of unlisted assets," said Howard Rosario, chief executive of Westscheme in Perth, 40 per cent of whose assets are unlisted. "How are we going to satisfy the need for precision that most people assume unitisation delivers?"