Superannuation Efficiency and Performance Unit Retirement, Advice and Investment Division
The Treasury
Langton Crescent
PARKES ACT 2600

19th April 2024

Dear Sirs,

Please find below our response as mailed on 19th April 2024.

We are an ASIC regulated placement agent business representing managers inside and outside of Australia with assets under management in excess of AUD300 billion. We work closely with APRA-regulated Superannuation funds and are pleased to provide our perspective on your consultation below.

Yours faithfully,

Uwe Fuehrer, CEO

Wealth of Nations Advisors Pty Ltd

1. Do you agree with these principles? Are there any other principles that should be considered?
    a. *Additionally, we believe in "Member Choice" as a core guiding principle to ensuring members have a say in how their superannuation fund is managed.*
2. Is assessing the implementation of a strategy, as opposed to assessing the choice of strategy itself, a strength or weakness of the current framework?
    a. *Undoubtedly a weakness, this creates the remarkable situation whereby a product with a superior investment strategy that delivers good returns may fail the test if the implementation of the strategy is below the benchmark.*
3. Can the existing methodology be materially improved, such as by further calibrating benchmarks, to largely address unintended consequences? How could these improvements overcome the incentive to benchmark hug, and remove barriers to invest in emerging asset classes?
    a. Benchmarking creates inherent issues in that certain investments do not align well to be benchmarking, particularly emerging assets. Many alternative and private assets have limited data points and irregular pricing. However, this doesn't negate their potential benefits to portfolios.
4. What asset classes do you consider require better coverage in the test? What asset classes are covered well by the existing test?
    a. *Alternatives investments for example are utilised globally by pension investors for their distinct risk and return profiles, yet benchmarking them remains complex. It's important to note that the methodology for benchmarking alternative investments is continually evolving; a fixed definition could swiftly become outdated and inaccurate.*
5. Do you consider additional indices covering additional asset classes should be added to the test? If so, please provide the following details for each of your recommendations:
        i. Description of asset class
        ii. Name of recommended index covering the above asset class, including the length of time data is available on the index
        iii. Details of appropriate fee and tax assumptions for such an asset class
        iv. Explanation of why you consider this index is appropriate for inclusion

    a. *As noted above there are substantial risks to benchmarking unlisted and alternative assets. Generally, risk-adjusted returns are globally utilised method for measuring the performance of assets. We see no reason why Australia should be diverge from global best practices in this regard.*
6. How should the test cater for new asset classes in the future?
    a. *Risk-adjusted returns are a globally accepted method of assessing new asset classes.*
7. Should the threshold for failure be recalibrated for some products? What evidence supports the need for a different threshold? How could a different threshold deliver better long term returns to members?
    a. *There is a danger in over complicated the threshold for failure. Additionally, further consequences may eventuate that are currently not contemplated. Our view is that following the reconsideration of benchmarking, the process for failure be re-assessed and until be placed on hold.*
8. Would retaining the current framework but moving to a simpler structure, such as a simple-reference portfolio of only bonds and equities, address some of the concerns with the current test?

   a. *This may work if only applied to bond and equities. Most super funds invest more widely to engineer optimal outcomes. We do not agree with this proposed approach.*

9. Would the Sharpe ratio be a more appropriate testing approach than the current framework? Would this lead to better member outcomes?
   a. *Yes. Trustees ought to contemplate the risk undertaken in pursuit of investment performance. Risk-adjusted returns stand as a well-established and comprehended cornerstone of the asset management sector. Consequently, referencing investment returns and their standard deviation should be deemed a basic prerequisite.*

10. How should the benchmark for performance be calibrated?
    a. *See above.*

11. What data should be used to estimate the Sharpe ratio, and how frequently?
    a. *The Share Ratio iis calculated by dividing the excess return of the investment (or strategy) over the risk-free rate by the standard deviation of those excess returns. Therefore, the data used in estimating a Sharpe ratio typically includes:*
       i. ***Historical returns** of the investment or trading strategy: These returns are usually calculated over a specific period, such as daily, monthly, or annually. They represent the performance of the investment or strategy over time.*
       ii. ***Risk-free rate:** The risk-free rate is the return on an investment with zero risk, typically represented by short-term government bonds or treasury bills. It serves as a benchmark for comparing the returns of the investment or strategy against a risk-free alternative.*
       iii. ***Standard deviation of returns:** This measures the volatility or variability of the returns of the investment or strategy over the same period used to calculate the returns. It quantifies the risk associated with the investment or strategy.*

12. 12. Are either of these approaches better than the existing test methodology (Option 1) or a simple Sharpe ratio (Option 2a)? Are there any other considerations that make this a better or worse option?
    a. *See above.*
13. Are there any other alternative single-metrics that would be superior in addressing the principles set out in this paper? How would they provide a better testing framework? What net benefits do they provide over other proposed metrics?
    a. *Not that we are aware of.*
14. What incentives would these alternative single-metric options provide trustees, and what would be the consequence of this for member outcomes?
    a. *Not applicable*
15. Would greater alignment to the APRA heatmaps improve the sophistication of the test?
    a. *We recommend caution on seeking to make the test more "sophisticated". The consequences of such an incorporation and the costs and practicalities of compliance would need to be carefully considered with an effort made to work through potential consequences that could effect optimal investment outcomes. The Heatmap approach is also backward-looking the focus on implementation means many of the outcomes of the current approach that have prompted this review are likely to be repeated.*
       Furthermore, the current APRA heatmap does not include any metrics of risk-adjusted returns, an approach that is widely seen as vital to optimal longer term member outcomes.

The mooted heatmap approach misses the mark on member-driven outcomes, particularly those around sustainability and represents an approach that rewards short-term financial gains.

16. Would it reduce incentives to benchmark hug and improve member outcomes?
    a. *See above.*
17. Is correlation between metrics an issue? If so, how should this be addressed?
    a. *See above*
18. Should the test capture all the metrics in the heatmap? If not, what metrics?
    a. *See above.*
19. How would the benchmark for performance be calibrated for chosen metrics? How would these metrics combine to determine overall pass/failure of the test?
    a. *See above*
20. What costs would be associated with aligning the test to the heatmap? What would be the benefits?
    a. *See above.*
21. Would this framework improve the sophistication of the test? Would it reduce incentives to hug benchmarks and improve member outcomes?
    a. *The three-metric test offers greater simplicity (when compared to the 8-metric option) and represents an opportunity to incorporate risk adjusted returns (net of fees). Provided this approach can incorporate an ability to follow sustainable investment strategies this could represent an improvement versus the current approach.*
22. Would this approach be more, or less, favourable than the heatmap approach?
    a. *Mnore favourable, provided widely accepted metrics are incorporated and sustainability outcomes can also be pursued.*
23. What would the costs of implementing this approach be? What would the benefits be?
    a. *We offer no comments on the costs, however we believe the benefits could result in more diverse and robust investment portfolios that provide better long term outcomes and better risk diversification.*
24. Are these the right measures of performance or are there other more important indicators of performance that should be measured in addition to or instead of those outlined? What metric should be used to assess these indicators?
    a. *No comment.*
25. How should the benchmark for performance be calibrated?
    a. *No comment*
26. How would an alternative framework be constructed according to the elements outlined above? Please provide specific details
    a. *Any framework should leave flexibility for faith, ethical and impact investments that widen investor choice and allow access to long term investment ideas that are nor constrained by inappropriate benchmarks. The prior test has reduced consumer choice in this regard and risks eliminating sustainable and impact-driven investing in Australia. This could be done as part of a qualitative overlay that allows Super funds wider discretion in implementing their investment goals.*
27. How would this framework more effectively advance the principles outlined in this paper?
    a. *Such an approach provides for more informed consumer choice in the market.*
28. What would be the costs and benefits associated with this framework, compared to the current test and any other alternatives?
    a. *The costs appear relatively low and rely on better reporting. This flexibility could be aligned with greater efforts to reduce greenwashing.*
29. What are the most important considerations for performance of retirement products?

   a. *Investment Returns: Generating consistent and competitive investment returns is crucial for the performance of retirement products like pensions and annuities. Factors like asset allocation, fund management, and risk management play a key role and can be assessed using risk-adjusted return measurement.*
   b. *Cost Efficiency: Keeping management fees and administrative costs low helps maximize the net returns to retirement savers but must be considered alongside the outcomes of the strategies. Lower cost and higher risk are not an acceptable outcome and returns net of fees are an important metric in a fair assessment.*
   c. *Longevity Risk Management: Effectively managing the risk of retirees outliving their savings is critical and should be measured in assessing the performance of super funds.*
   d. *Inflation Protection: Ensuring retirement incomes keep pace with inflation is important and again can be measured.*

30. If the test were to expand to retirement products, would they require a different test to the accumulation phase? Would the test differ for different retirement products
   a. *No comment*
31. How could longevity products be most appropriately assessed? How could the products be compared?
   a. *No comment*
32. Do you agree that retirement phase, single-sector and externally-managed products are suitable for testing? Why or why not?
   a. *No comment*
33. Should different assessment methods be applied to different cohorts of products?
   a. *No comment*
34. Do you agree that the 'other products' outlined above are unsuitable for testing? If you think the 'other products' (or a sub-section of these products) are suitable for testing, ho could they be appropriately tested.
   a. *No comments*
35. Under each design option, how could the test accommodate cohorts that are suitable for testing? For example, using different metrics or benchmarks for performance for different cohorts.
   a. *No comment*
36. 36. How should fees be measured under each design option?
   a. *No comment*
37. Should fees be measured at the current option level, or should they be measured on a different level? How would this be achieved?
   a. *No comment*
38. Are the current assumptions made in comparing fees acceptable? For example, should the $50,000 representative member balance be adjusted based on the median member balance for a product cohort?
   a. *No comment*
39. Is a peer comparison of fees the best way to measure fees? Is there a better approach to benchmarking fees? If so, how should this work?
   a. *No comment*
40. What product cohorts should be considered? How should different cohorts be defined where products could meet multiple cohort definitions, such as single-sector retirement products?
   a. *No comment*
41. How many years of of fees data is appropriate to test? Should a greater weighting be given to certain years?

   a. *No comment*

42. Should the consequences be adjusted to improve outcomes for members? How would this need to be tailored for the different options for performance testing?
    a. *Given the extent of consolidation in the industry further forced mergers may leave investors without appropriate levels of choice. Fines and other levies could be considered provided these are not taken from member funds. One option would be to have senior executive compensation vested for a longer term and forfeited if long term investor outcomes are not met. This works well in the private sector where aligning intertest between investors and those investing the funds is a key consideration for investors in selecting an investment manager.*
43. How should the consequences be amended to better account for edge cases or different cohorts that fail the test for reasons beyond the trustee's control?
    a. *No comment*
44. How could these provisions be effectively ring-fenced so that it applies only to the edge cases and not failures at large?
    a. *No comment*
45. How could this be achieved without subjecting the regulator to undue challenge and impacting the efficiency of the regime?
    a. *No comment*

46. What other remediation processes could occur?
    a. *No comment*
47. Are there any key barriers to consolidating closed and underperforming products? What quantitative evidence is there of these barriers? How do these weigh against other reasons a person may choose to remain in a product?
    a. *No comment*
48. What evidence do trustees use to demonstrate that remaining in a closed and underperforming product is in the best financial interests of members, compared to moving to a performing product?
    a. *No comment*
49. What is the process or criteria that trustees use when deciding on what product they will transfer members to when consolidating underperforming products?
    a. *No comment*
50. Should APRA receive increased regulatory powers to direct superannuation trustees to consolidate underperforming products?
    a. *No comment*