From: grow@marinisgroup.com.au
Sent: Friday, 14 December 2018 2:37 PM
To: Alex Wiedenmann | Marinis Group
Subject: I love a challenge
Attachments: 2018 07 31 _ How super funds play the ratings game _ Stockspot.pdf; 2018 10 01 _ Creating a fairer superannuation balance _ EUREKA published.pdf; 2018 11 05 _ When your balanced super tips too far to riskier side.pdf; Media Release No 85 _ 2018 09 06 _ A Super Mess.pdf; Media Release No 86 _ 2018 09 08 _ The super mess we need sorted.pdf

eGrow - December

Dear Friends,

I love a challenge

Those of you who know me well, will attest to this fact.

Well, I was recently thrown a challenge by a client whose numeracy skills I hold in high regard. He wanted to be able to rank the performance of his family self-managed super fund (SMSF) relative to a range of investment alternatives, to determine if they were invested in the right investment mix.

In meeting that challenge, there were a number of issues arising from the process which are worthy of sharing, if not reinforcing, with our eGrow readers:

- Return on investment is dependent on the level of risk we are willing to accept and therefore the level of exposure to growth assets that we are willing to accept to achieve higher returns.
- There is an often-misunderstood aspect of wealth creation, we are all investing in the same underlying assets – it is just the mix that is different. There is no standard definition, agreement or regulated definition on what constitutes a 'Growth', 'Balanced' or 'Moderate' portfolio.
- NO ONE can achieve higher returns in the long run without exposing a portfolio to greater risk, even though unfortunately, many try to give the impression that they can and are! That is why the adage "The greater the risk, the greater the return" remains true.
- Our job at Marinis Financial Group (MFG) is to design and implement the strategy based on the 'investment risk' profile and preferences of our clients (while at the same time keeping costs low, using 'best-of-breed' products). We also strive to maximise our clients' opportunities within superannuation laws, at the interface of the ATO, and where appropriate, Centrelink.
- The Banking Royal Commission has really grabbed people's attention, super and pension fund members are demanding to know that they are being charged the right amount and that they are getting the services they pay for. I say this is a great outcome – plus I am happy to say that since Marinis Financial Group achieved our Financial Services Licence, we have been able to drastically reduce costs by negotiating wholesale investment product pricing for our clients, and this lower cost base is very attractive.
- Providing for retirement via your own Self-Managed Super Fund (SMSF) is not for everybody. As we all know, fees matter. Unless the total balance in the fund is significantly large enough to provide sufficient economies of scale, an SMSF can be a relatively expensive proposition. As well as the additional financial costs of reporting and audit requirements, there is the time cost of SMSF management, even with the professional support of accounting and financial planning advisers. It is possible to achieve similar returns using retail super funds, at a considerably lower cost.
- You have probably heard or read my comments that the main reasons, in my view, for a family to use an SMSF is when they have a direct investment property (or share portfolio) – or to facilitate an inter-generational wealth transfer. If any of these are a consideration in your retirement mix, then an SMSF may be appropriate.
- It is worth bearing in mind too, that where there is a direct property in an SMSF, valuations are difficult. The approach taken will have a direct impact on how the overall portfolio performance is measured. My dad used

to say that you only really know what a house is worth on the day it sells; and we are all aware that real estate values are currently experiencing what would appear to be a temporary downturn.

The back story:

My clients' SMSF includes a commercial investment property, making a performance comparison against the benchmark performance for a similar asset mix an extremely difficult task – futile, in fact, if attempting to make comparisons using various retail and industry funds as a benchmark reference.

Nevertheless, it became an academic challenge, based on my research and that of my team, to test whether it was possible to provide a meaningful performance measurement. As well as performance, the measurement also needed to be made in the context of a review of the efficacy of the fund's direct property investment, and full consideration of the SMSF costs.

After interrogating a series of investment databases and comparison charts, we were able to provide a very detailed comparative performance analysis (relative to the correct performance benchmarks) of the returns achieved, less costs incurred, for each financial year since 2014 when MFG was appointed as advisers.

The bottom line:

Whilst it is neither appropriate nor practical to reproduce full details of our findings via this forum, the bottom line outcomes confirmed that the investment strategy was on the right track. The results are summarised (with permission of our client) below:

Based on MFG's recommended 'Balanced' investment strategy (65% Growth, 35% Defensive asset exposure) the portfolio achieved:

- An average return over 4 years (for the period 30 June 2014 - 30 June 2018) of 8.8% pa.
- 1-year return (after fees) to 31 August 2018 of 11.99%

This one year return compared favourably to the one year benchmark return for a Balanced Index ETF portfolio (to 31 August 2018) of 13.00% (based on Vanguard's slightly more aggressive 70% Growth, 30% Defensive asset exposure).

This slightly lower return was also commensurate with the slightly more defensive MFG definition and asset allocation for a balanced portfolio.

Whilst this 'best of breed' SMSF administration service does not provide volatility figures, the Vanguard 70% Growth, 30% Defensive Index with a with a 3-year Standard Deviation of 5.48% can again, be used as a reasonable proxy.

The slight performance gap was cost competitive, given the complex portfolio structure of the SMSF and the accompanying administration costs, which are ranked 'best of breed' in terms of SMSF administration.

Calculated as a percentage of the total portfolio value, the total cost of SMSF administration plus ALL investment costs (including the direct property) was an extremely cost effective 0.23% pa. Excluding the direct property, total costs came in at a very competitive 0.35% pa.

Overall, the conclusions drawn from our analysis were that the portfolio has performed very favourably in terms of investment returns and costs.

It also served to reinforce MFG's role over that 4-year period – which is essentially to design and implement investment strategy based on our clients' appetite for risk and investment preferences, as cost effectively as possible. It is then up to the market, and the specific asset allocation/exposure to the different asset classes which will determine the actual returns on investments.

There will always be highs and lows in investing. I encourage people (particularly in the super draw down phase) to plan for a 5.0% pa return – even though in this example the return was 11.99% for the year to 31 August 2018, and 8.8% pa since 1 July 2013.
This is what I call the 'magic pudding' zone – where you spend your 5.0% but see your investments growing!

And one more thing:

If you are interested in MFG's approach to investment over the last decade and a half, I encourage you to fossick through our bank of Media Releases (MR) and statements on our website www.marinisgroup.com.au.

And another thing… if you would like to see my comments in the media over the last month or so, please see attached documents. In particular, I draw your attention to:

MR 85 "***A Super Mess***";
MR 86 "***The Super Mess that needs to be sorted***";
Eureka contribution 1 October 2018 ***"Creating a fairer Superannuation Balance";*** and
Money Saver HQ 5th November 2018 "***When your Balanced super tips too far to riskier side."***

These media contributions were influenced by the challenge outlined above. It dawned on me then that there is an incredible amount of confusion out there – making it hard for the average super fund member to compare apples with apples in the super space!

As ALWAYS, please don't hesitate to get in touch if I, or any of our hard-working team can do anything for you.

Kind Regards,

Theo Marinis B.A., B.Ec., CPA., FPA®
Financial Strategist
Authorised Representative

GROW @ Marinis

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Creating a fairer superannuation balance

Creating performance league tables won't rectify the super mess.

Summary: The Productivity Commission will play a central role in the development of superannuation fund performance league tables.

Key take-out: The bigger issue is creating standard definitions for the different asset allocation terms being marketed.

The flaw in the superannuation system revealed by the Royal Commission is the fact that few people actually understand the complexities or issues of what we have.

And what we have is a mess which allows marketing spin and self-interest to distract long-term investors away from the sole purpose of superannuation – to provide funds for retirement.

The mess starts at the top. The very senior bureaucrats in Canberra who are advocating significant change to the industry are the people who invented the system we are suffering under. Now they are advocating new ways of looking after savings by appointing the Productivity Commission to a new oversight position.

Appointing the Productivity Commission to be the arbiter of the top performing funds 'hit parade', or league table, is mindbogglingly foolish.

For a start, there is an absolute conflict of interest for these public servants, who along with our politicians are entitled to a defined benefit pension in retirement, while the rest of us 'civilians' are left trying to decide which 'fund' performed best.

Instead of developing a league table, the Productivity Commission should be creating a clear understanding of superannuation terminology – and publishing that information. We need to compare apples with apples.

Industry funds, retail funds and self-managed super funds (SMSFs) are just tax structures which allow us to invest in the same underlying assets. Some structures cost more and some cost less – and some have different functionality – but that is a minor issue. The major issue is that Canberra senior bureaucrats should not be cheerleading for any structure, super fund or super sector.

What is vitally more important is for superannuation members to clearly understand how their money is allocated – but I haven't heard anything from the Commission or its proponents about this.

The Productivity Commission should actually set specifications for the various asset allocations labelled 'Defensive', 'Conservative', 'Moderate', 'Balanced', 'Growth', and 'High Growth' by (a) asset class and (b) their appropriate weightings to growth vs defensive assets allocations for each defined profile.

If the Productivity Commission is given these 'league table' ranking responsibilities, we will find ourselves wading through a new Royal Commission in the next decade as those who were burnt by the top 10 league chart put pressure on politicians to answer questions about why their investments underperformed.

There seems to be a collective 'take-out' from the Royal Commission that somehow industry super funds are 'good' and that retail super funds and SMSFs are 'bad'.

Recent media reports state that industry funds are currently recipients of transfers from retail funds, which all plays well to a narrative that there is good and bad amongst the various methods of superannuation funding.

If we are to be black and white, industry funds are not the cheapest form of super fund available, they are not the most flexible, and they don't have the best insurance options. But they are still good. The same can be said for retail funds and SMSFs.

What we need to consider is the make-up and investment approach all funds adopt and look across the same skyline.

In other words, use a mandated description of what constitutes a certain style of investing. We need appropriate benchmarks, so we can all really compare the performance of a particular fund to the right benchmark for a designated risk profile.

And we don't need self-interested senior bureaucrats trying to pick the winning superannuation fund of the future!

No one can do that, least of all the senior bureaucrats and their masters in Canberra.

Theo Marinis

More articles from Theo Marinis ›

When balanced super tips too far to riskier side

ANTHONY KEANE

VOLATILE financial markets are set to pressure Aussie savers to question just how risky their superannuation fund's balanced investment option is.

Big variations in asset mixes within funds will cause some members to worry about what's in their nest egg.

A majority of workers' super is in default balanced funds, which official figures show comprise an average 70 per cent growth assets, such as shares and property, and 30 per cent defensive assets, such as cash and bonds.

However, Marinis Financial Group managing director Theo Marinis said some balanced funds were a "wolf in sheep's clothing" because they comprised up to 90 per cent growth assets.

"Any link with a balanced fund profile is tenuous," he said.

A large market correction would result in "massive underperformance" by so-called balanced funds that were really growth funds, Mr Marinis said, so members needed to know just how their money was invested.

We're five months into the 2018-19 financial year and the nation's biggest balanced super funds have a negative year-to-date investment return after sharp falls in shares. Their high growth options have fallen further, and even their conservative investment options are negative, hit by low interest rates. Rainmaker Information, the research group behind the SelectingSuper fund comparison service, defines a balanced portfolio as having between 55 and 75 per cent in growth assets.

Its executive director of research, Alex Dunnin, said there were several definitions of "balanced" but none were universally accepted.

"Yes, the term is very confusing. But before we get too excited, the issue only matters if you're trying to compare funds or decompose why they did well or didn't," he said.

Many people did not care too much about the term "balanced", Mr Dunnin said, and simply wanted their fund to invest for good long-term returns without taking on excessive risks. "Recently, some people in superannuation have been saying balanced funds should be a 50:50 mix between growth and defensive assets, but that would make for very conservative portfolios."

Mr Marinis said the Productivity Commission should set rules to define investment profiles, such as "balanced", "conservative" and "high growth".

"The potential for people to rely on terms which are fundamentally misleading should be removed," he said.

But Mr Dunnin said national rules were unlikely. "If we can't agree on the formal definition of what a free-range egg is, how will we be able to define what a 'balanced' portfolio is?"

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Media Release No 85 **6th September 2018**

A Super Mess

By Theo Marinis

The flaw in the superannuation system revealed by the Royal Commission is the fact that few people actually understand the complexities or issues of what we have. And what we have is a mess which allows marketing spin and self-interest to distract long-term investors away from the sole purpose of superannuation – to provide funds for retirement.

The mess starts at the top. The very senior bureaucrats in Canberra who are advocating significant change to the industry are the people who invented the system we are suffering under. Now they are advocating new ways of looking after savings by appointing the Productivity Commission to a new oversight position.

Appointing the Productivity Commission to be the arbiter of the Top Performing Funds 'hit parade', or League Table, is mind-bogglingly foolish.

For a start, there is an absolute conflict of interest for these public servants, who along with our politicians, are entitled to a defined benefit pension in retirement, whilst the rest of us 'civilians', are left trying to decide which 'fund' performed best.

Instead of developing a league table, the Productivity Commission should be creating a clear understanding of superannuation terminology - and publishing that information. We need to compare with apples.

Industry funds, retail funds and Self-Managed Super Funds (SMSFs) are just tax structures which allow us to invest in the same underlying assets. Some structures cost more and some cost less – and some have different functionality – but that is a minor issue. The major issue is that Canberra senior bureaucrats should not be cheer leading for any structure, super fund or super sector.

What is vitally more important is for superannuation members to clearly understand how their money is allocated – but I haven't heard anything from the Commission or its proponents about his.

If it is to really add value to society, the Productivity Commission should actually set specifications for the various asset allocations labelled 'Defensive', 'Conservative', 'Moderate', 'Balanced', 'Growth', and 'High Growth' by a) asset class and b) their appropriate weightings to Growth vs Defensive assets allocations for each defined profile.

At the moment, there are no clearly defined benchmarks for these so-called asset allocation profiles – which means they are used more as marketing terms than as indicators of the level of investment risk and appropriate investment timeframes. As such, these labels are fundamentally misleading – and perhaps conveniently so.

To demonstrate this farce, leading Industry super fund and Productivity Commission hero HostPlus is currently able to market a fund as a 'balanced' portfolio when the asset allocation has a ratio of 90-98% growth asset exposure. *

Small wonder then, with markets booming, that the HostPlus 'Balanced' fund was the best performer in 2018!

In actual fact, this fund is a 'high growth' wolf, masquerading in sheep's clothing - designed to give members a false sense of security for a VERY aggressive portfolio.

This scenario also brings to mind the example of the MTAA Super Fund, which in 2008, just before the GFC, was ranked the best performer in 2008 (no doubt the Productivity Commission would have placed it top of the table as one of the best performing funds if it were charged with the proposed responsibility at the time).

Unfortunately for MTAA and its members, when the GFC hit, the fund lost $1.5 billion of members' cash because of being too heavily weighted in growth assets when the market cracked. *

This is often what transpires, when higher and higher returns are the focus with little regard for the associated risk.

It is my contention that if the Productivity Commission is given these 'League Table' ranking responsibilities, we will find ourselves wading through a new Royal Commission in the next decade as those who were burnt by the top 10 league chart put pressure on politicians to answer questions about why their investments underperformed. The Productivity Commission will replace APRA and ASIC in the 'frame'.

There seems to be a collective 'take-out' from the Royal Commission that somehow Industry super funds are 'good' and that Retail super funds and SMSFs are 'bad'. Recent media reports state that Industry Funds are currently recipients of transfers from Retail funds, which all plays well to a narrative that there is good and bad amongst the various methods of superannuation funding.

If we are to be black and white, Industry Funds are not the cheapest form of super fund available. Industry Funds are not the most flexible and they don't have the best insurance options. But they are still good. The same can be said for Retail funds and SMSFs.

What we need to consider is the make-up and investment approach ALL funds adopt and look across the same skyline. In other words, use a mandated description of what constitutes a certain style of investing. We need appropriate benchmarks, so we can ALL really compare the performance of a particular fund to the right benchmark for a designated risk profile. And we don't need self-interested senior bureaucrats trying to pick the winning superannuation fund of the future!

NO ONE can do that, least of all the senior bureaucrats and their masters in Canberra.

Theo Marinis is Managing Director of Marinis Financial Group

* Read here: Stockspot Blog 'How super funds play the ratings game' by Chris Brycki

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Media Release No 86 **28th September 2018**

The super mess we need sorted

By Theo Marinis

One of the biggest challenges for members of super funds is they can't reliably compare them – and it is up to the Productivity Commission to fix this situation, says Adelaide based financial strategist Theo Marinis.

The solution, however, does not lie in publishing a league table based on performance, without providing members with some understanding of the how each of the super funds invest their members' money – and how this fits with the labels under which they are marketed.

Host Plus, for example, currently offers a 'Balanced' portfolio which has a 90% allocation to growth assets (generally Australian and international shares and property).* With the majority of the portfolio exposed to growth assets, to my mind and the industry's standard definitions, any link with a 'balanced' fund profile is tenuous. In fact, this is really a 'high growth' fund with all the inherent volatility risks.

It is little wonder, then, with markets booming, that Host Plus was the best performing in the 'Balanced' fund sector in 2018.

This is just one example of the marketing spin that has crept into the superannuation system.

Under the present Productivity Commission recommendations, we may well find that funds like the Host Plus are placed on top of any performance League Table – with the result that trusting consumers attracted to the performance and the position on the table would be likely to pile in - falsely reassured by the marketing label 'Balanced'.

When the market inevitably corrects, however, many of those members who redirected their super to this fund are also likely be shocked by a massive under-performance and reduction in their account balance because their 'balanced' fund was really a 'high growth' fund. In other words, a wolf masquerading in sheep's clothing - designed to provide a false sense of security for a VERY aggressive portfolio.

In 2008 the MTAA super fund was also a top performer – until the GFC stripped $1.5 billion of member assets.* Massive reversals are possible in difficult times, so consumers need to know what fund they are actually buying into. A typical balanced fund has a more conservative spread of assets to reduce the scale of any declines.

To really help consumers the Productivity Commission needs to make some rules which define the parameters for investment profiles currently marketed as 'Defensive', 'Conservative', 'Moderate' 'Balanced' 'Growth' and 'High Growth'. And these definitions must have as their basis a) the exposure to each asset class (e,g. shares, property, fixed interest and cash); and b) the appropriate weightings to growth and defensive assets. With industry funds you can't "compare the pair" when each fund can decide what is an apple and what is an orange.

If someone wants to invest in a high growth fund, because it suits their timeframe for investment and they are comfortable with riding out market downturns, that's fine. But the potential for people to rely on terms which are fundamentally misleading (i.e. when 'balanced' really means 'high growth' and therefore find their super savings exposed to higher than expected market volatility) should be removed.

'Our authorities should be doing all they can to make super understandable to the average worker – without the marketing spin,' Theo Marinis said.

Theo Marinis
Managing Director of Marinis Financial Group

* Read here: Stockspot Blog 'How super funds play the ratings game' by Chris Brycki

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How super funds play the ratings game (Part 1)

31 July 2018 (https://blog.stockspot.com.au/how-super-funds-play-the-ratings-game/) Chris Brycki (https://blog.stockspot.com.au/author/chris/) Financial advice (https://blog.stockspot.com.au/category/financial-advice/), Investing (https://blog.stockspot.com.au/category/investing/)

It's that time of the year again when super funds release their annual performance. This blog looks at how the funds twist their performance relative to other funds and indexing. The funds' PR is parroted by the ratings agencies whose tables and good news story are accepted at face value by the media.

Firstly, we look at how funds manipulate their inclusion into the categories set by the ratings agencies.

Defensive assets

ASIC defines defensive assets as cash or government bonds.

Cash is defensive because when market fall it holds its value.

High grade bonds can do one better and rise when share markets fall. History backs this up too; in each of the 6 times Australian shares had a down year in the past 20, bonds rose to cushion the impact.

Can other assets be defensive?

This very much depends on the opinion of the fund manager and there is strong history to demonstrate why their opinions might not end up as fact.

High income stream and low growth assets

Just because an asset delivers a big income stream does not make it defensive. Take Telstra. Most of Telstra's returns come from regular fully franked dividend income but its share price has dropped 60% since 2015.

Infrastructure and property assets

Much infrastructure and property is held in unlisted vehicles which raises 3 concerns:

- The value of the investment is the opinion of the fund manager and there is no way of knowing whether that value is credible given that there is no open market for the asset.
- The financial structure may see a return of capital reported as an income distribution.

- The investment is very illiquid and a sale is often extremely constrained by agreements with co-investors, including first right of refusal and so-called 'tag-and-drag' conditions. One critical characteristic of a defensive asset is to be able to sell it in a deep and open market.

The inherently risky nature of these investments is usually exposed towards the end of each market cycle when too much debt is loaded in to beef up returns. In 2008 the Real Estate Investment Trust (REIT) sector fell by a whopping 75% globally because these funds had created income which couldn't be sustained under high debts and falling prices.

During the Financial Crisis some super funds stopped members from transferring money out because they were unable to sell illiquid unlisted assets. One fund, MTAA super, lost $1.6 billion due to poor hedging of unlisted assets (https://www.theage.com.au/business/super-fund-controversy-highlights-the-need-for-greater-transparency-20110609-1fuvw.html). MTAA super lost its spot as one of the best performing funds in 2008 to become the second worst according to Super Ratings.

Creative definitions of defensive assets

In recent times many super funds have invented their own definition of a defensive asset which has helped to push them up the ratings.

Let's look at this year's top performing fund, the Hostplus default balanced fund which claims a 24% allocation to defensive assets.

The Hostplus website (https://pds.hostplus.com.au/5-how-we-invest-your-money) explains that in addition to cash and fixed income "some asset classes, such as infrastructure, property and alternatives may have growth and defensive characteristics".

Their self-defined defensive assets include infrastructure, credit, property and alternatives. These makes up 22% of the 24% portfolio allocation to defensive assets. Government bonds make up just 2% and there is zero cash!

Hostplus default balanced fund

DEFENSIVE ASSET	PORTFOLIO ALLOCATION
Infrastructure	5%
Credit	6%
Property	9%
Alternatives	2%
Fixed income	2%
Cash	0%
Total	**24%**

Source: Hostplus

This has enabled Hostplus to claim top gong in its chosen category.

Hostplus isn't the only one. Many of the top funds on this list have counted some other assets as defensive to make the *Balanced fund* weigh-in.

Top 20 performing balanced funds over 1 year to 30 June 2018

FUND & OPTION	RETURN OVER 1 YEAR
HostPlus – Balanced*	12.5% p.a.
AustSafe Super – MySuper (Balanced)	11.4% p.a.
AustralianSuper – Balanced	11.1% p.a.
Cbus – Growth (Cbus MySuper)*	10.9% p.a.
Club Plus Super – MySuper	10.8% p.a.
Equip MyFuture – Balanced Growth	10.7% p.a.
Sunsuper for Life – Balanced	10.7% p.a.
HESTA – Core Pool	10.6% p.a.
NGS Super – Diversified (MySuper)	10.5% p.a.
UniSuper Accum (1) – Balanced	10.5% p.a.
Mercy Super ASG – MySuper Balanced	10.4% p.a.
Intrust Core Super – MySuper	10.4% p.a.
Vision SS – Balanced Growth*	10.4% p.a.
QANTAS Super Gateway – Growth	10.2% p.a.
First State Super – Growth	10.2% p.a.
Media Super – Balanced	10.1% p.a.
CareSuper – Balanced	10.1% p.a.
Aust Catholic Super & Ret – Growth	10.1% p.a.
LGIAsuper Accum – Diversified Growth*	9.8% p.a.
Catholic Super – Balanced (MySuper)	9.8% p.a.
SR50 Balanced (60-76) Index	**9.2% p.a.**

*Interim results only

Source: SuperRatings

This prompted me to ask Hostplus CIO Sam Sicilia the following question:

Chris Brycki @chrisbrycki · Jul 30

Thanks for the reply Sam. What measure/s do you use internally to determine if an asset qualifies as defensive? Where can members find more info on the underlying investments and return history of the assets that make up the defensive 24% inside the Balanced option?

1

Sam SICILIA
@SamSicilia

Follow

Replying to @chrisbrycki @David_Elia_ and 2 others

Chris - every asset has a growth and defensive characteristic. There are simply too many assets to detail the capital (growth) and income (defensive) characteristics of each. It suffices to say tha it is possible (albeit laborious) to do the math at the individual asset level.

11:55 AM - 30 Jul 2018

The Productivity Commission got a similar response from many super funds when asking about returns for individual assets. Only 5 of 208 funds were prepared to disclose them.

Unfortunately, super funds aren't required to disclose how they classify their investments on their website or to anyone. Not to members, to the Australian Prudential Regulation Authority (APRA) or ASIC! They also aren't required to share how each asset has performed or even what it is. This allows funds to play the ratings game without anyone holding them to account.

By all means Hostplus and other funds should be free to invest in illiquid unlisted infrastructure, alternatives and property assets.

Just don't call them defensive!

How Hostplus sells the 'success' of its balanced default fund

Hostplus chief executive David Elia puts the performance down to **active management (https://www.afr.com/personal-finance/find-your-super-fund-in-the-top-performers-20180725-h1340k)**:

"Over the past three years our balanced option did 10.16 per cent, while the index balanced option did 7.29 per cent, so that's almost a three percentage point differential. The [active] balanced option has outperformed across every time horizon" he says.

It's absurd that Hostplus compares its indexed balanced option which has 25% cash and bonds to its default balanced option with just 2%.

It would be fairer to compare it to an index fund with a similar amount of risk. For example, the Vanguard High Growth Fund has a 10% allocation to cash and bonds and generated the following returns over 1, 5 and 10 years after fees and taxes.

	HOSTPLUS BALANCED DEFAULT (2% BONDS AND CASH) 1.45% p.a. INVESTMENT FEE	VANGUARD HIGH GROWTH (10% BONDS AND CASH) 0.29% p.a. INVESTMENT FEE
1 year	12.5%	11.9%
5 years	11.0%	11.1%
10 years	7.4%	7.7%

Performance is net of investment fees and tax. Vanguard returns are for a super fund paying tax in accumulation stage.

Source: Chant West, Vanguard

When comparing much more similar funds, Hostplus performed **just below** an index fund over 10 years. That's not bad, most funds did a lot worse!

How ratings agencies support the misleading self-reporting

The ratings agencies don't properly query the allocations reported by the funds. This provides no check as to the real risk of the self-reported defensive assets.

In addition, the ratings agencies have a few additional problems of integrity which we discussed in what fund ratings won't tell you (https://blog.stockspot.com.au/what-fund-ratings-wont-tell-you/). To recap:

- Most ratings businesses only publicly announce the top performers and not the worst. This is because they are typically paid by the funds who they rate. Anyone who has seen The Big Short (https://blog.stockspot.com.au/lessons-i-learned-from-the-big-short/) would understand how problematic this conflict of interest is. It's why we publish the Fat Cat Funds Report (https://www.stockspot.com.au/fatcat/) to shed a light on the best and worst funds.
- Performance over 1 and 3 year periods is meaningless yet it becomes the major focus each year. You need to see how a fund has performed over a full market cycle (around 10 years) to have any idea how it performs in good and bad times.

Active or indexed super?

By our analysis (which we'll share in Part 2 of this series), over 90% of active super funds **underperformed an index fund of similar risk** over 5 and 10 years after fees and taxes.

Expensive fees for active management is precisely what causes most super funds to underperform. For every active winner there has to be an active loser (https://blog.stockspot.com.au/why-you-wont-beat-share-market/) and management fees drag down net returns.

There are always going to be a small number of funds who beat the index but that group is always changing. Many funds in the top lists this year have also spent time near the bottom when markets weren't as kind to them.

Winners always change. Fees are with you every year.

How to pick the right super fund

For those looking for a super fund with a low allocation to defensive assets, Hostplus might be one to consider. Let's be clear, Hostplus and other Industry funds are making some good investments including into venture capital and infrastructure projects that will benefit Australia.

However what shouldn't be making headlines and driving members to switch is how the fund performed compared to lower risk options in a rising market.

Chasing the latest returns harms investors

Over the last 10 years Hostplus has been one of the very few funds to **almost**
generate enough extra returns to match an index fund of similar risk. Vanguard's high growth fund still beat it by 0.3% per year after fees and taxes over 10 years.

Compared to the disastrous bank owned retail super products (https://blog.stockspot.com.au/fat-cat-report-5-years/), industry funds consistently come out ahead. However that doesn't mean some stakeholders aren't massaging the truth about what drives returns and therefore what's in the best interest of members.

Will Hostplus be able to keep up with an index fund over the next 10 years? Maybe, maybe not. Based on history, the odds of a fund that charges 1.45% per year beating a low cost index fund across the market cycle is not high. Warren Buffett proved this when he recently won a 10 year bet that a Vanguard index fund would beat 5 expert-selected active fund managers.

Buffett backed the index fund which won by a massive 77%.

Look out for Part 2…

In Part 2 of this series we look at how to pick a super fund based on the 2 factors within your control and proven to drive return: risk and costs.

Each year our Fat Cat Funds Report (https://www.stockspot.com.au/fatcat/) shows that these 2 factors are by far the most important. Focusing on risk and cost rather than ratings and fund manager storytelling will help you cut through the spin and find a fund with the best chance of success.

Grow your savings the smart way

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