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More opting to manage their own superannuation

James Dunn | *August 20, 2008*

IT is hard not to draw the obvious conclusion from a slumping share market in 2007-08, resultant negative returns from superannuation funds and growth in numbers of self-managed superannuation funds (SMSFs).

More people want to go it alone managing their super. Statistics released by the Australian Prudential Regulation Authority (APRA) in June show that the number of SMSFs grew in the March 2008 quarter from 372,481 to 378,656, with a total of 730,000 individual members.

SMSFs now hold $289 billion, or 26 per cent of the nation's $1.1 trillion super pool. The average member balance is $435,000, much larger than the average for corporate super funds ($100,000), public sector funds ($62,000), retail super funds ($24,000) and industry super funds ($19,000).

The market downturn since November "would have played a big role" in the growth of SMSFs, says Phillip Le Greca, technical services director at specialist SMSF administrator Multiport.

"Every time there's a share market dip and the public-offer super funds start to show poor returns, historically there is a surge in the number of SMSFs. By definition, self-managed super fund operators are self-motivated people. Poor super fund returns seems to spark a feeling among such people of 'Why am I paying these people to make a loss? I could do better than this'."

For such people, there was plenty to grumble about last financial year.

According to superannuation research house Super Ratings, the average balanced super fund -- the category that holds more than 80 per cent of Australians' super -- lost 6.4 per cent for the financial year, the first negative return in six years. And those grumbles might have translated into action if the self-motivated investor had seen the results of a survey of 500 SMSFs conducted by research firm Investment Trends, looking at the 12 months to May 2008.

The survey found that the returns (self-assessed and after costs) of the funds averaged 14.2 per cent, with 19 per cent of respondents indicating that their fund had produced a return of between 20 and 29 per cent -- figures the passive fund members could only dream about.

Investment Trends principal Mark Johnston says the sample is a "representative sample of the SMSF market", but cautions against "drawing definitive conclusions" from it.

"Firstly, the study represents how respondents estimated their returns at the time. It's perceived return -- they're not marking-to-market as the public-offer super funds do, so it really shouldn't be compared against actual super fund performances, which most certainly do mark to market.

"The second caution I would make is that if you look at the index, June was actually when most of the damage was done. In the year to May, the share market was down about 8.5 per cent, but in June it dropped a further 11 per cent, so the self-assessed returns might not have been as positive if we'd talked to the sample a month later."

Johnston adds that there was a "strong trend" in the survey where the SMSF respondents stated they were carrying paper losses but had no intention of selling the assets. "There were very few who said they had realised losses as a result of the market volatility, or who intended to sell perceived risky assets and move to safer assets. Most of them had used the market downturn to buy assets at good prices."

Johnston expects to see an increase in interest in people setting up SMSFs in the wake of the public-offer funds falling into the red -- and the results of his own firm's survey -- but says converting that to action in establishing an SMSF depends on how long the market stays down.

"In the last bear market, which ran from March 2002 to March 2003 (when the market lost 22 per cent),

there was a big spike -- about 50 per cent -- in the establishment rate of SMSFs. But the key issue is that it has to be a long bear market, because when that happens people can see successive negative annual returns on their super fund -- which can push many people who were thinking about an SMSF to start one."

Andrea Slattery, chief executive of Self-Managed Superannuation Professionals Association of Australia (SPAA), hopes not to see a "knee-jerk reaction" of people pouring into self-managed super because public-offer funds had a financial year in the red.

"We don't actually want to see the SMSF industry flourishing for the sake of it. We want people that fit the right purpose and the profile for these particular funds to be the ones going into them, and we also want the appropriate people to be giving them advice.

"There's a lot of research data showing the SMSF market to be quite a reasonable performer, both in times that have been very good and in times that have been a bit tougher. If you wanted to look at more empirical data, the APRA Report on Fees and Performance, which came out in December 2007, showed that in the eight years to December 2005, small APRA funds (superannuation funds with less than five members that are subject to prudential regulation by APRA) outperformed the market -- that is, the other areas of superannuation -- in six of the eight years, and did so by between 1 to 6 percentage points.

"The small APRA funds are effectively the same as SMSFs, but they're about 0.5 per cent more expensive than SMSFs to run -- so you could say that the SMSFs outperformed the other super funds by an extra 0.5 per cent on top of the small APRA funds' outperformance."

Simon Makeham, principal of SMSF specialist advisory firm Makeham Financial Services, says an SMSF should not be benchmarked against the share market index, and nor should it measure itself against the balanced super funds' medium to long term benchmark return of "CPI plus 3.5 per cent" a year.

"That type of benchmarking works for public-offer and industry funds, but an SMSF operator needs to look at their investment objectives and understand what the fund is trying to achieve.

"By and large, public-offer funds are restricted to a particular suite of investments, being managed funds, shares, property and bonds.

"The whole point of an SMSF is that it does not have to be based on the traditional asset classes. Traditional asset classes come about by way of a limited investment choice that some of the major funds can offer. It would be difficult for them to administer, across thousands of members, some investments that you can undertake through an SMSF environment."

Benchmarking returns also depends on the time line of the SMSF investment, he says. "We don't advocate moving away completely from traditional asset classes, but we say that by using an SMSF, you are better positioned to make alternative-type investments. For example, we have a number of people who are invested in an art trust. It's a unitised trust that invests in a collection of works by a reputable artist.

"That's an exotic investment, an alternative asset class, but it's still an investment that complies with the super law, and is undertaken for the right reason -- to generate capital growth to provide income in retirement. That's a long-term investment, but an SMSF is something that can be used for future generations.

"It's not a vehicle that you're investing in purely for mum and dad today. The investment choices that you make within that fund can be to provide for future generations as well.

"That's how you should be thinking, as opposed to outright benchmark returns. And generally speaking, our funds outperform CPI plus 3.5 per cent by a long shot."

Slattery says the SMSF sector is "too big to ignore". Research modelled by the SPAA projects that in 2021, SMSFs will hold $1.5 trillion and represent 34 per cent of the $4.3 trillion super kitty -- the largest chunk.

After empirical research by Monash University and Trowbridge Deloitte, some industry participants

predict that super in future will comprise industry funds and SMSFs -- leaving corporate, public-sector and retail funds to join the former or wither on the vine.

But Slattery believes that "there's room for all the models". While she says that people managing their retirement is a more accepted phenomenon, there will always be those who are not interested.

"Somebody who is interested in far more options and permutations, and who doesn't wish to manage super themselves, will still want to be willing to be involved in a retail fund," Slattery says.

"There is the need for the niche that the industry funds have provided and the niche that the retail funds have provided. And while you've got big companies who want economies of scale, the corporate funds will be able to keep their patch. It's just going to be a lot more evenly spread."

At the end of the day, she adds, nobody in the super industry should be talking about making inroads into others' patches. "We don't need to, because we've got 9 per cent growth every year."

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