Superannuation: Inspiring excellence

2015 ASFA/PwC CEO Superannuation Survey

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"There needs to be a target of adequacy that all Australians should try to achieve and policy settings should allow for people to push to obtain (a comfortable lifestyle under) the ASFA Retirement Standard."

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Executive summary

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Welcome to the fourth annual ASFA/PwC CEO Superannuation Survey, which captures the opinions of more than twenty of our industry's leaders across a range of topical issues. As in prior years, this survey covered the matters on the minds of the CEOs in relation to:

- strategic priorities over the coming years
- investment approach and management
- operational matters including the impact of regulatory reform, data quality and member advice.

Consistent with the 2014 CEO Survey, post retirement products and digital strategy remain at the top of funds' three year strategic plan and are consistently considered as emerging risks within the industry. Post implementation of the new Superannuation Prudential Standards, the last two years has seen a renewed focus on member engagement, advice offerings and operational efficiency. The top three emerging risks are investment performance, digital disruption and strategic innovation.

CEO's believe that their funds have been successful in embedding strong risk cultures within their operations, underpinned by well-developed management of risk appetite. Linked to the risk management within their funds, over 70% of the CEOs funds have met their Operational Risk Financial Reserve target in advance of the three-year transitional period. The majority of the CEOs, however, are of the view that there is further work that could be done with regards to these reserves to make them more relevant to their fund's needs and risk profile.

CEOs believe that the introduction of SuperStream and MySuper have not yet delivered the expected reduction in the operating costs across the industry and the associated decrease in member fees. They are also of the view that there will be no reduction in the level of administration costs seen in the next three years given the investment in technology that has been required. Linked to SuperStream, data quality has been a topic for discussion throughout the industry in recent times and CEOs are confident that the quality of their data is increasing and are having minimal issues with the data received through SuperStream.

From an investment governance perspective, the continued development of product dashboards and enhancements of investment management frameworks has brought a greater focus on the investment objectives of funds. There is also a shifting focus towards other investment management issues in the medium term, with CEOs citing social impact investing and the role of venture capital and private equity as being important investment management issues moving forward.

Pauline Vamos

CEO, The Association of Superannuation Funds of Australia

David Coogan

National Superannuation Leader, PwC

Highlights

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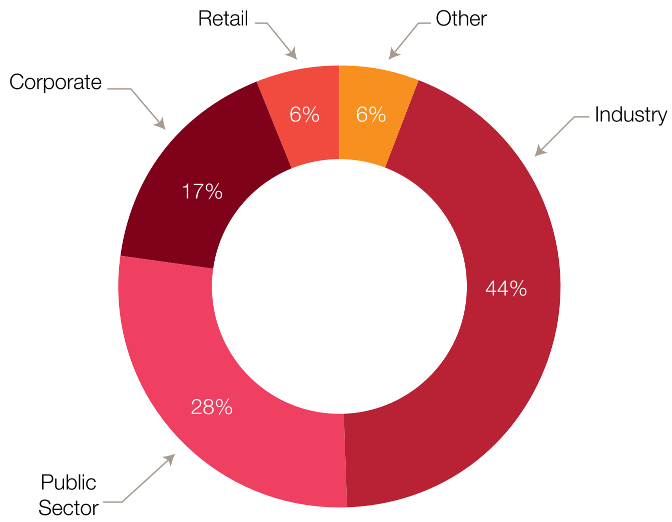
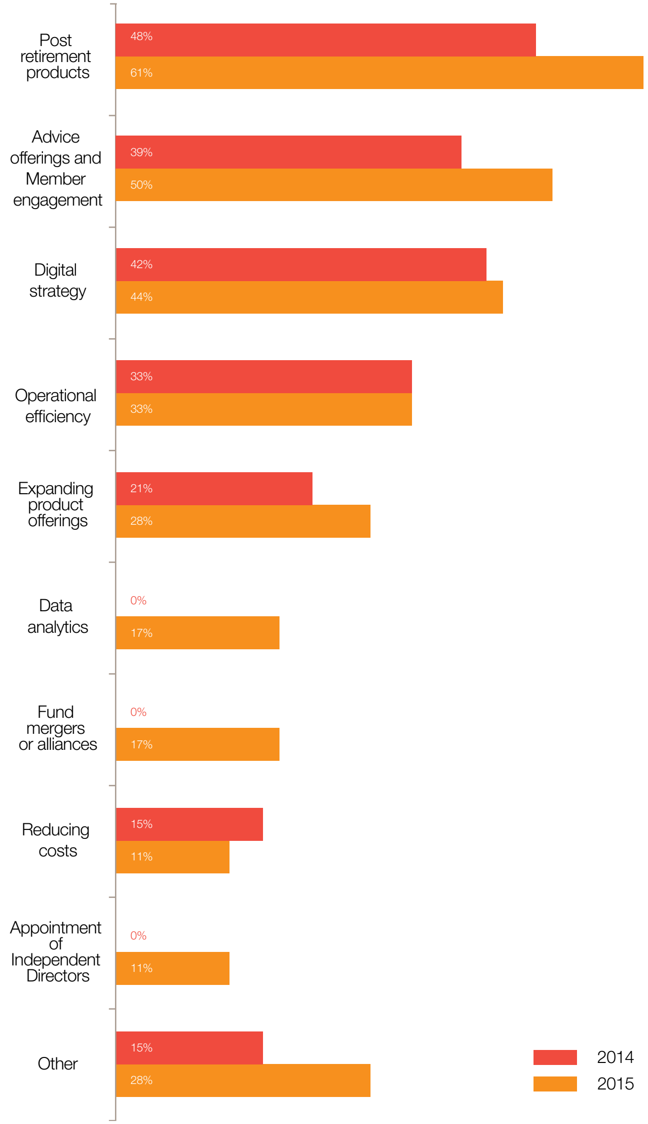
What is the sector of your fund?



What are your key strategic priorities in the next three years?



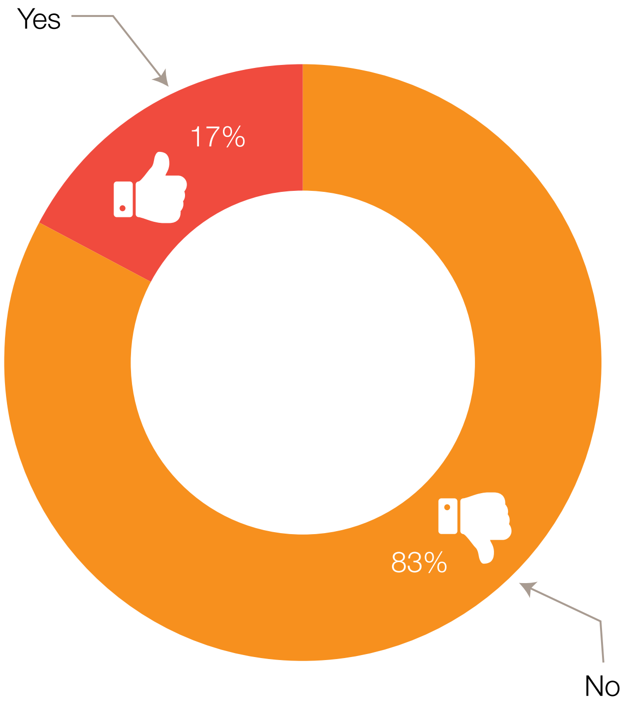
What are your top three emerging risks for your fund in the next three years?

Investment performance
50%

Digital disruption
44%

Strategic innovation
44%

Are you looking to appoint additional independent directors in the next 12 months?



"High level objectives establish boundaries for Government policy and give certainty to funds to enable them to set their longer term business strategies."

Strategic priorities

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Consistent with the 2014 survey, post-retirement products and digital strategy remain as key strategic priorities to focus on for the next three years. Linked to the need to develop post-retirement products, member advice also remains a significant priority.

Now that the Superannuation Prudential Standards and associated regulatory changes have been embedded into day-to-day activities, operational efficiency has re-emerged as a significant priority for fund CEOs. The fact that these regulatory changes are now part of business as usual has also had a positive impact on the quality of the data held with more than half of the respondents seeing an increasing level in data quality.

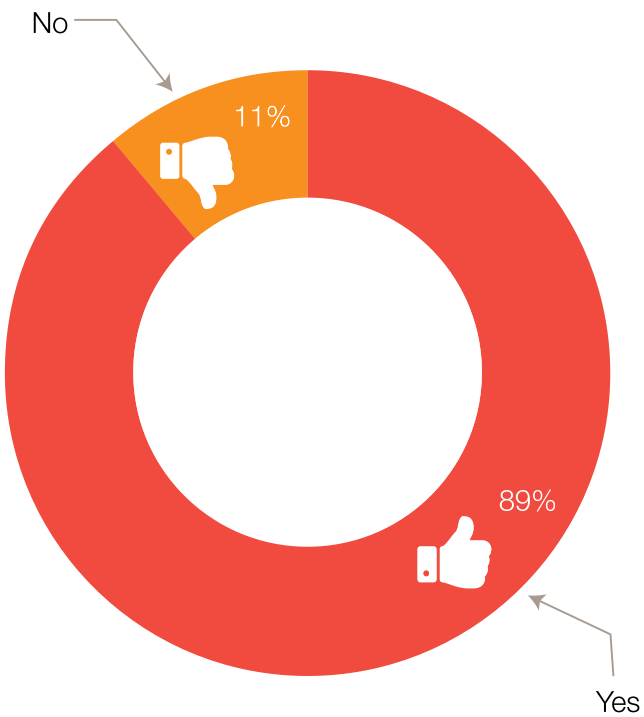
The challenge on the regulatory front for most CEOs is to translate these changes into operational efficiencies and reduce ongoing operational costs of the funds and, flowing on, fees charged to members.

As we look beyond 2015 and towards the outworking of the Financial Services Inquiry (FSI), the appointment of independent directors will likely become an increasing focus for CEOs. For the moment, however, this remains a watching brief and an area of lesser priority for funds.

89% of the CEOs consider that there should be high-level objectives set for superannuation and retirement income, with the view being that the purpose of superannuation has been forgotten and that too many consider it to be a wealth accumulation vehicle rather than a retirement income stream. There is a belief that by setting high-level objectives, boundaries are established for Government policy which in-turn provides certainty to superannuation funds to establish their longer-term business strategies.

"The basic objective is to deliver the best net return over the long term and anything more than that creates complexity and leads to unintended consequences."

Do you consider that there should be high level objectives set for superannuation and retirement income?



1. Post retirement products

With the Australian population steadily aging, for the second year in a row post retirement products continue to emerge as the highest rated key strategic priority in the next three years by the CEOs surveyed.

Research continues to show that along with global ageing trends, Australia will follow a similar pattern and we are not only living longer, but are also working longer.

- the over 45s population is expected to grow by 4 million to over 13 million in the next twenty years;
- one in two people will be aged 45 or over and one in 25 will be aged 85 or over by 2034; and
- the over 50s demographic hold over 60% of the $1.8 trillion wealth invested in superannuation today and it is this cohort of the population who will inevitably draw down on that wealth in the next few decades and will need heightened attention and advice.

This presents significant opportunities for growth in both the provision of advice and financial products and it also provides superannuation funds the opportunity to develop 'cradle to grave' investment product options.

Whilst there is a sound business case to justify strategic decisions around further developing post retirement products, the reality for most Australians is that they will not have a sufficient superannuation balance to independently fund their retirement and a significant number will therefore be reliant on the Aged Pension. This reliance will be to varying degrees and the research suggests this cohort will look to spend the early years of their retirement in part-time work, leisure and investment activities which will be replaced by longevity, health and aged care priorities in later years.

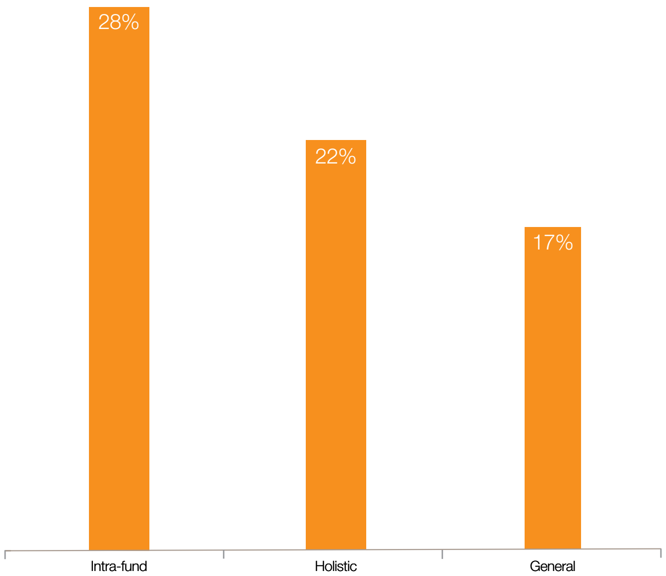
2. Advice offerings and member engagement

The need to provide sufficient financial advice to members goes hand-in-hand with the development of more post retirement products. Therefore, it is no surprise that advice offerings are rated as the second highest strategic priority of the CEOs surveyed in 2015.

Due to the numerous regulations around superannuation funds, there is an opportunity for the industry to be viewed as trusted advisors to members and help them in navigating the complexity of decisions required to secure their financial future.

Based on the survey responses, CEOs have noted that the main type of advice currently being provided to members is intra-fund advice, with the focus of the member being on resolving problems with their own account rather than seeking assistance with future financial needs.

Type of current member advice offering



In the previous two years, 80% (2014) and 65% (2013) of CEOs said that the number of members seeking advice was increasing. With this increase being felt, the focus shifts to the different channels through which advice can be provided.

More than 60% of the respondents stated that they are planning to put income projections onto their member statements, and the increase in the use of digital tools has seen the initial development of Robo Advice channels within the industry.

Whilst there is some support for the MySuper product dashboard, 71% of those responding to the survey felt that the dashboard is not utilised by members and does not serve as a true decision-making tool when it only applies to MySuper options and does not also consider the other investment choice options available to members.

However, the responses show that the more traditional approach towards member engagement is still more broadly favoured, with CEOs placing targets more on attendance numbers at seminars and the number of financial planning meetings held rather than the number of app visits or Robo Advice usage. This is likely to change as funds embrace the digital age.

3. Digital strategy

Digital strategy has remained as one of the three highest key strategic priorities for the next three years according to the survey results, having been rated as the second highest strategic priority in 2014.

Superannuation funds without a digital strategy are at risk of not keeping pace with the way the industry is headed. Superannuation funds should also be looking to implement a social media policy if they have not done so already and explore opportunities to engage with members on social media platforms.

Many corporations in other industries have found success utilising the power and influence of social media and have been able to interact with customers in personal and engaging ways that were unimaginable only a short time ago through a number of strategies including dedicated Facebook pages, live online support and competitions. Being seen as accessible and approachable will be important attributes that funds will need to demonstrate as they look to execute their digital strategy and broaden their online presence in a competitive industry.

Despite assumptions about how members in certain age demographics prefer to engage with funds, not all members in these demographics are similar and funds need to consider further understanding their members' needs and wants to shape their communication strategies. Organisations will need to adapt to maintain their competitive advantage in the next decade regarding responding to the needs of older customers.

This includes realising that the over 45s do not all have similar characteristics and are at different stages of their retirement journey. They are increasingly tech-savvy and are predicted to be big users of digital and mobile technologies which will shape how super funds seek to effectively engage with members and attract new members.

One of the key risks to consider when determining a digital strategy is cyber threats. With cyber threats impacting virtually every sector across the globe over the last 12 months, these risks are no longer an issue concerning just IT and security professionals; the impact has extended to the boardroom, contact centre and beyond. Technology breakthroughs will likely help superannuation funds reduce the complexity of cyber security, more quickly detect and remediate incidents, and improve their ability to monitor and analyse digital activity. As our industry evolves into an interconnected business ecosystem through the use of digital innovation and the implementation of SuperStream requirements, the superannuation industry requires a shift from security that focuses on prevention and controls to a risk-based approach that prioritises a superannuation fund's most valuable assets and its most relevant threats.

The PwC 2015 Risk and Compliance Benchmarking Survey, undertaken across the investment management and superannuation industries, highlighted that over half of the respondents did not have a written cyber or privacy incident management and response plan. A further 24 per cent of these respondents are not planning to develop one soon.

Having a robust privacy and cybersecurity incident management or response plan is essential to mitigate the severity of an incident as it occurs. In the event of an incident, the lack of a planned response may result in significant financial and reputational damage. With the ever rising costs of privacy and cybersecurity incidents, CEOs and trustees should no longer see having an incident management/response plan as an option, but as a necessary control to mitigate potential risks.

When it comes to investing in digital trust, despite the belief in high value returns, the PwC 2015 Risk and Compliance Benchmarking Survey results indicate that 88% of respondents have set their privacy and cybersecurity budget for FY15 as less than 1% of their revenue.

This is consistent with the global trend amongst financial services firms. The PwC 2015 Global State of Information Security Survey showed that security spending amongst financial services institutions has not kept pace with the rise in security incidents and costs, as security spending for financial services organisations has stalled at less than 4% of the total IT budget for the past seven years.

With the budget allocation constituting only a small percentage of organisational revenue streams, the lack of resources available to increase the privacy and cybersecurity budget further increases the risks of not having the appropriate controls and remediation plan in place to manage privacy and cybersecurity risks.

Data quality and administration costs

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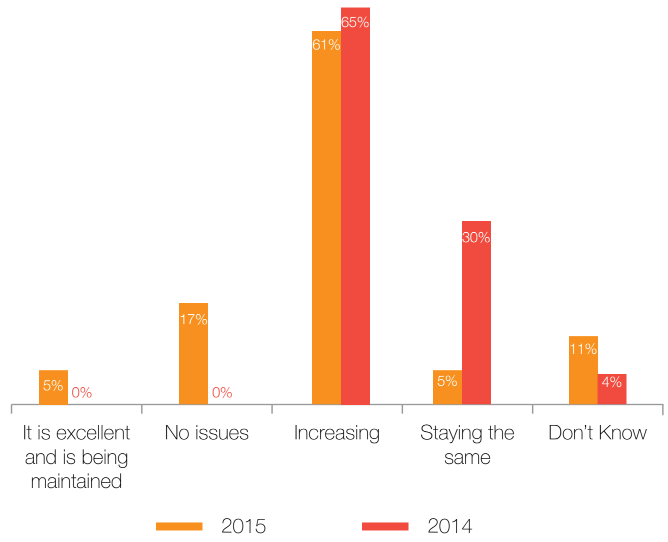
Consistent with the 2014 survey, in which 65% of respondents rated their data quality as having improved, 74% of CEOs believe that the quality of their data has continued to improve in 2015. The CEOs also had very positive comments in relation to SuperStream, with 79% noting that they were experiencing few difficulties with the data received through the SuperStream channel.

When asked about the implementation costs of SuperStream, 67% of the CEO’s surveyed spent less than $1 million, 22% spent between $1 million and $5 million and the remaining 11% spent greater than $5 million.

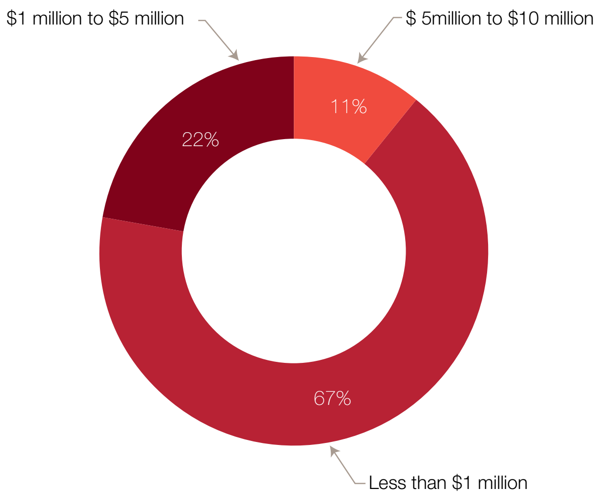
It is interesting to note from the responses received by the CEOs that this continually improving quality of data has not, to date, led to efficiencies from an operating cost perspective. It is not expected that any such gains will be made within the next three years, with 68% of CEOs commenting that they anticipate their administration costs will stay the same or increase over that time.

When CEOs were asked whether current disclosure requirements for fees and costs are working well, 56% answered no, with the underlying theme being that members are not able to compare ‘apples with apples’ due to inconsistent interpretations of the disclosure requirements within the industry. There is a consistent view being expressed by the CEOs that the focus should be on net returns rather than fees.

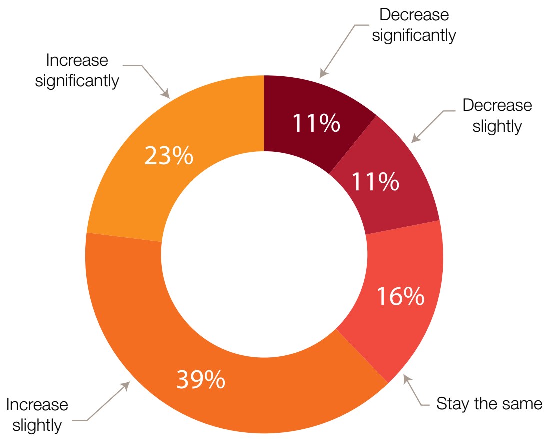
Changes to levels of data quality

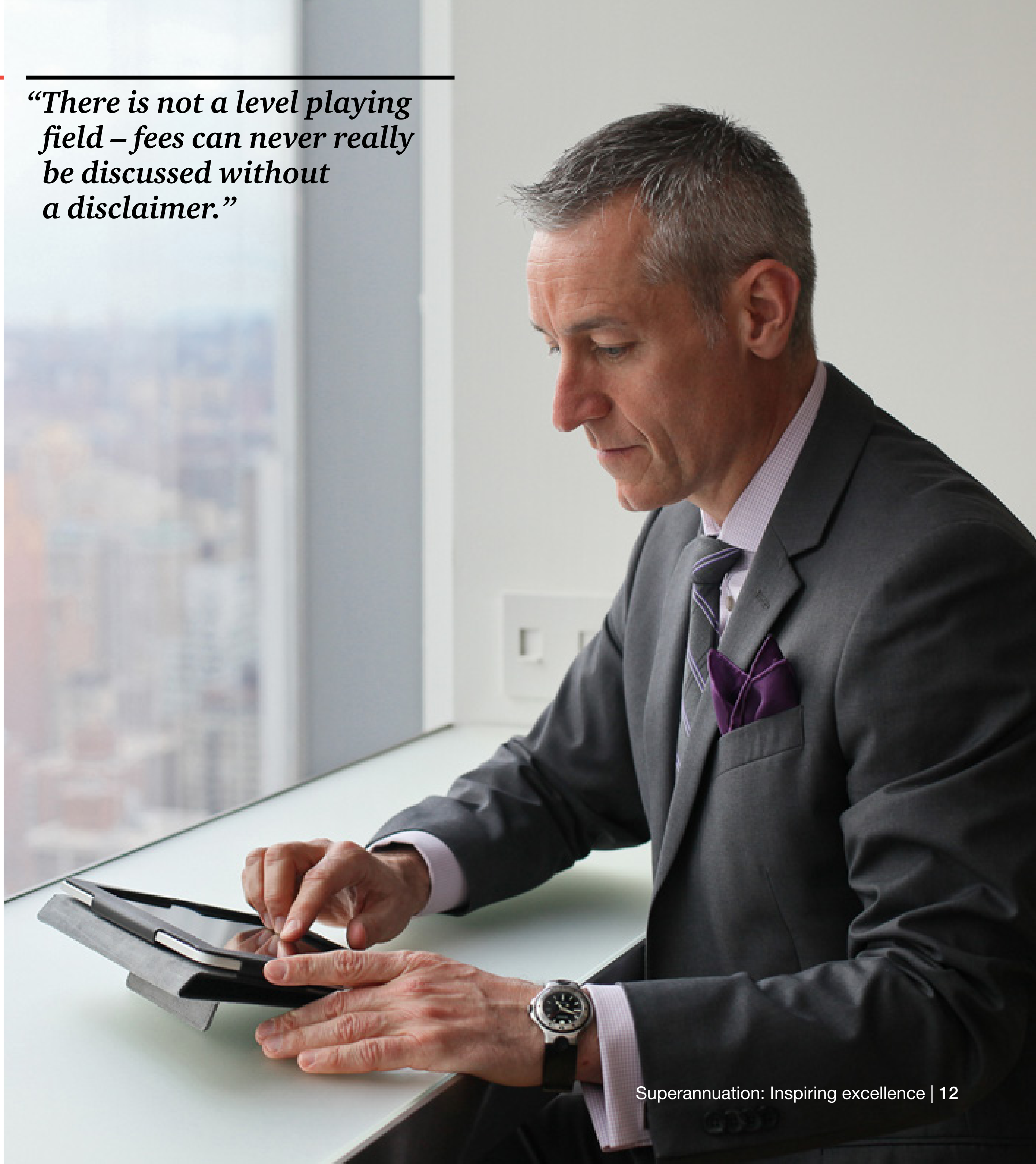


SuperStream implementation costs



Anticipated changes to administration costs in the next three years





"There is not a level playing field – fees can never really be discussed without a disclaimer."

Investment management

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In the 2014 survey, we reported that funds were recruiting talent from investment managers to provide uplift to the internal investment governance and management capability. Last year, 70% of the CEOs surveyed did not intend to insource their investment management function over the next three years. Having decreased from 77% in 2013, this number has decreased again in the 2015 survey, with 63% of the respondents not intending to increase their in-house capabilities in the investment management space.

As in prior years, CEOs explained their decision not to insource their investment management due to the limited size of operations and a desire to continue to access manager expertise. For those CEOs who are looking to bring more capabilities in-house, the key drivers are to take ownership of more operational-type activities and to manage assets at a lower cost.

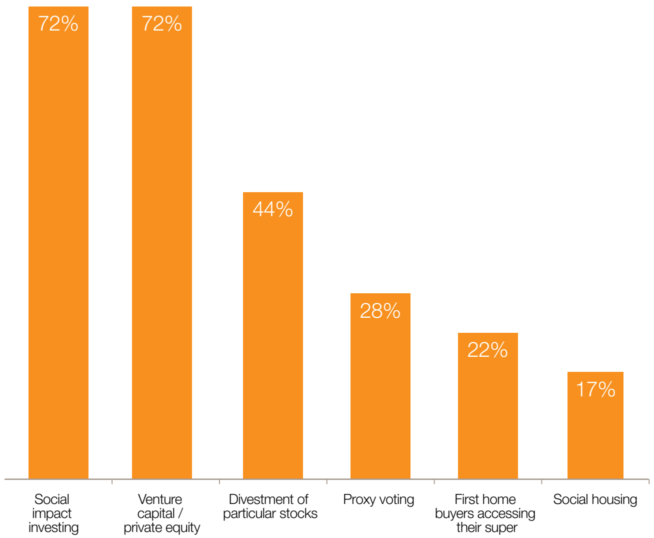
Following on from the Cooper Review and associated Stronger Super reforms, the introduction of *SPS530 Investment Governance* has placed a greater focus on the articulation and communication of investment objectives to members. Whilst there is some variation in the investment objectives set by funds, in the main it is clear from the responses that almost all funds have chosen to implement a CPI plus a fixed percentage return. The jury is still out when it comes to the development of lifecycle and age-based investment objectives, with only 17% of the respondents having aged based or lifecycle objectives.

The same can be said for goals-based investment objectives, where only 33% of the respondents are following this approach. Interestingly, though, a number of other funds are considering going down this route in the future.

When looking at the most important investment management issues in the medium-term, there was a general consensus that there needs to be more of a focus on issues around societal relevance and areas that matter to their members, with 72% of responses focussing on the need for investment strategies to consider social impact investing.

There is also a significant focus on the role of venture capital and private equity within the investment management space in the medium term, 72% of responses also highlighting this as a key investment management issue. The total value of Australian mergers and acquisitions and private placement deals rose by 70% for the year ended 30 June 2015 (source: Australian Private Equity and Venture Capital Association Limited). This provides a further opportunity for funds to diversify their portfolios away from traditional listed equities and fixed interest securities.

What are your three most important investment management issues in the medium term?



Risks and reserves

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83% of the CEOs who responded to the survey believe that they have a well embedded risk culture and a well-developed risk appetite.

This is somewhat at odds with commentary from APRA, who have stated that some in the industry have yet to demonstrate that they have a sound understanding of the difference between risk management and compliance and that there is scope for Boards to further enhance risk appetite statements to achieve more balance between qualitative and quantitative assessment of risk (source: APRA Insight, Issue One 2015).

Linked to their risk culture and risk appetite, 72% of the CEOs commented that their fund has met their target Operational Risk Financial Reserve within the three year transition period mandated by the Superannuation Prudential Standards. This is despite 61% of the respondents declaring their disagreement with the minimum requirement. The key driver behind the disagreement relates to the reserves not appropriately reflecting the risks facing the funds. 68% of the CEOs would support a more risk based approach to setting these targets.

There is a general consensus amongst the respondents that there should be high-level objectives set for superannuation and retirement income and that by doing so this may build more confidence within the industry and remove the politicisation of superannuation. Setting high level objectives will establish boundaries for Government policy and provide more certainty to funds to enable them to set their longer term business strategies.

Have you met the 25bps ORFR minimum target?

Yes

72%

Do you agree with the ORFR minimum?

No

61%

About the survey

The ASFA/PwC Survey 2015 was sent to the CEOs, of all of the major superannuation funds, in September 2015. Respondents represented the views of a wide range of organisations across the superannuation sector including industry, retail, corporate and government funds.

This report provides an overview of the survey findings together with analysis and interpretation of the results. We have also included some direct quotes from CEOs throughout the report. These quotes reflect the respondents' opinion and reflect the passion felt on each issue we asked. These views are not necessarily consistent with the overall survey findings.

We thank the CEOs who participated for their time and insights.

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