

Super Returns

– putting them into perspective

ASFA Background Paper
August 2008

Returns for the year to 30 June 2008

There has been a lot of turmoil in the Australian and overseas investment markets over the past year or so due to factors such as repercussions from the credit crisis in the US and the continuing increases in the price of oil. This has resulted in negative returns on sharemarkets around the world, including Australia, for the year ended 30 June 2008.

Although superannuation funds generally offer members the option to select an investment strategy that meets their risk profile, most superannuation fund members are in portfolios that invest approximately 65% to 75% of their assets in shares and property. The balance is invested mainly in fixed interest and cash. Further, many of these portfolios have between 60% and 70% of their assets invested in a combination of global and Australian sharemarkets.

The names given to these type of portfolios vary, but generally they have been called balanced, or at times, growth portfolios. For ease we shall refer to them as balanced.

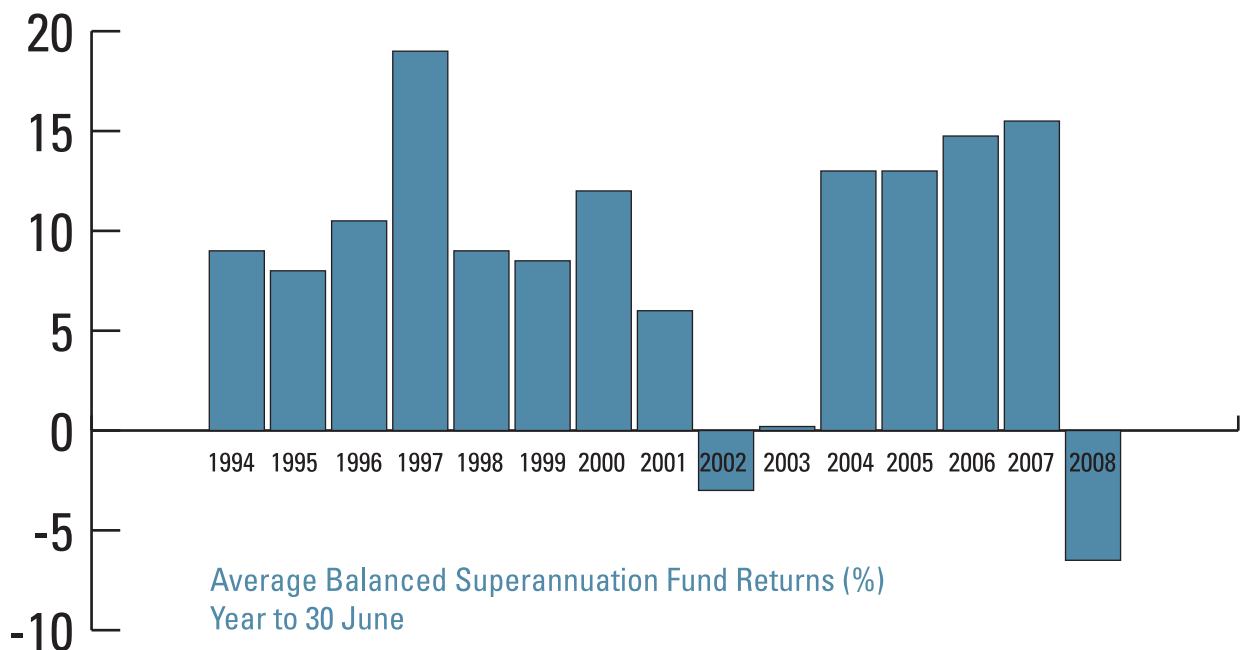
Over the year to 30 June 2008 global and Australian sharemarkets have decreased in value returning around -21% and -14% respectively. Over the same period cash returned around 7% with fixed interest returns generally below those of cash. Under these conditions it is of no surprise that many balanced superannuation portfolios produced negative returns for the year.

Occurrence of negative annual returns

It is not unusual for portfolios that have at least 60% invested in sharemarkets to produce an annual negative return every 5 or 6 years. In fact, following a preceding long period of relatively strong annual returns, such as that to 30 June 2007, there is some likelihood that another negative return may follow for the financial year to 30 June 2009. However, there is also a likelihood that the annual return to 30 June 2009 will be quite a reasonably positive result. That is, markets are not predictable.

We show below balanced portfolios' financial year returns over the past 15 years.

(A table containing financial year returns over the past 40 years is included in the appendix to this paper.)



Note: The annual returns over the past 7 years have been derived from the median returns in the SuperRatings surveys for balanced portfolios and from the ChantWest multi-manager surveys for growth portfolios. SuperRatings is a member of ASFA and Warren Chant is a member of ASFA. Annual returns longer than 7 years ago have been largely derived from average returns of funds participating in various surveys.

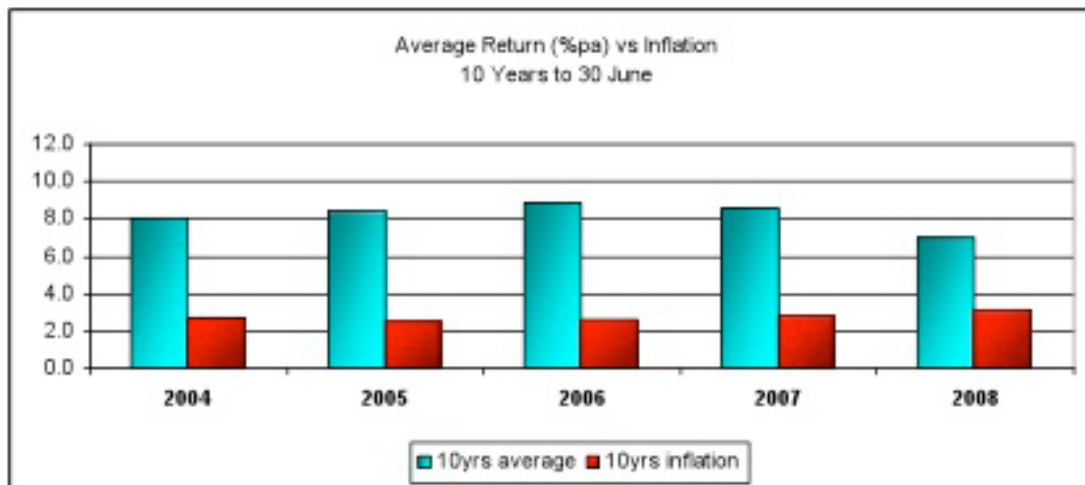
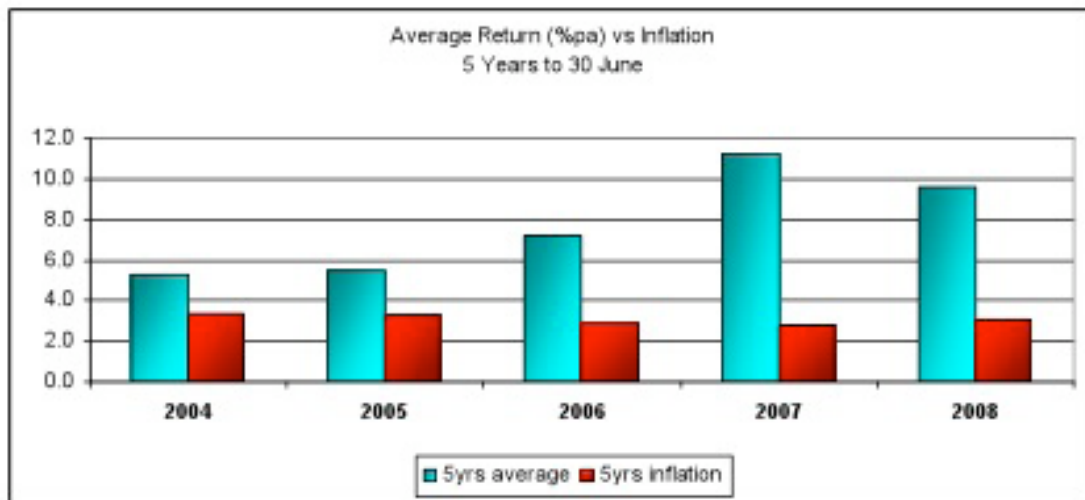
There have been two negative financial year returns experienced by the above balanced portfolios over the past 15 years (and one very low return of 0.1% for the year to 30 June 2003). So why invest in such portfolios, that is, portfolios that have such a large exposure to sharemarkets? The answer is that, over a longer period, such portfolios are expected to provide much higher returns than portfolios that consist of less in sharemarkets and more in cash and fixed interest.

Superannuation funds and long term returns

Superannuation funds have been designed to allow members to contribute to their fund during their working lives so that they can reap the monetary benefits during retirement. Therefore, for most members, it is a long term savings mechanism. For some members, that are nearing retirement and will need to draw on their superannuation monies, it is a shorter term savings mechanism.

Generally, balanced portfolios within superannuation funds have been designed with the “average” member in mind. That is, a member that still has a relatively long time frame over which contributions will be made and over which any account balance can accumulate. Therefore, balanced portfolio returns should be viewed over the longer term. It should be recognised, however, that over shorter term periods these portfolios may experience low, and at times, negative annual returns.

We show below how balanced funds performed over past 5 and 10 year periods and compare these to inflation rates as measured by increases in the Consumer Price Index. The same scale has been retained to assist comparability. (Tables showing returns from 1 July 1968 over rolling 5, 10, 15 and 20 year periods compared to increases in inflation and to increases in average weekly earnings are included in the appendix.)



Note: The annual returns over the past 7 years have been derived from the median returns in the SuperRatings surveys for balanced portfolios and from the ChantWest multi-manager surveys for growth portfolios. SuperRatings is a member of ASFA and Warren Chant is a member of ASFA. Annual returns longer than 7 years ago have been largely derived from average returns of funds participating in various surveys.

Although past returns are not a reliable predictor of future returns, the above longer term returns do illustrate some of the smoothing effects that are expected by taking a longer term view. They also confirm the expectation that balanced portfolios' returns provide a respectable margin above increases in inflation over the longer term.

Finally we note that most superannuation funds also accommodate members that are other than “average” or those who wish to design, to an extent, their own portfolios, by allowing the members to select different portfolios to the balanced fund. Some of these portfolios have more in sharemarkets, some have less while others may have no exposure to sharemarkets at all.

Funds’ product disclosure statements (PDSs) set out the investment options available to members. They also set out the objectives of each option and a suitable time-frame over which an option should be considered. Generally, when a PDS outlines that a particular investment option should be considered over the long term it means that members should expect low or even negative annual returns from time to time. Further, that investment option is expected to produce a higher return over the longer term than an investment option that is to be considered over the short or medium term.

It is important to make sure that you are invested correctly and contribute accordingly to achieve your desired retirement outcomes from your superannuation. It is also important to understand that investments that have higher expected long term returns also have higher expected variability of returns, and even negative returns, in the short term

Therefore, a negative annual return for a superannuation investment option that is suitable for longer term investors should not be automatically viewed as a cause of alarm. Rather, it may be viewed as the price paid to achieve a higher longer term return.

Where to from here?

Last financial year’s negative returns should not be used as a trigger to change your superannuation investment strategy. Rather, if you are unsure about the continued suitability of some aspects of your superannuation fund’s structure or investments, it should be used as a catalyst to obtain more information and clarity.

A suitable process would include the following:

- Review your superannuation fund’s PDS and review your understanding of the various investment options available to you.
- Review whether your investment strategy and contribution rate continue to be appropriate to meet your monetary objectives for retirement. Younger members usually may take a longer term view than members nearing retirement.
- Do you wish to have the same investment strategy for your account balance and future contributions?
- Don’t forget to take all costs, including switching investment strategies and/or switching superannuation funds into account.
- If you are not sure or wish to seek clarification on some of the information in your superannuation fund’s PDS seek professional advice – your income in retirement is at stake!

Appendix – Balanced Fund Returns

Annual Financial Year Returns over the past 40 years

Year Ending 30 June	Average Fund Return(%)	CPI Increases(%)	Wage Increases(%)
1969	8.3	2.5	7.5
1970	-1.5	3.0	8.4
1971	2.4	4.7	11.2
1972	20.6	7.2	10.2
1973	0.1	5.7	9.0
1974	-14.5	13.2	16.2
1975	8.7	16.5	25.4
1976	21.3	13.0	14.3
1977	7.3	13.8	12.5
1978	15.5	9.5	9.9
1979	13.9	8.2	7.7
1980	37.5	10.2	9.5
1981	17.1	9.3	13.9
1982	-2.8	10.5	14.6
1983	26.4	11.4	11.4
1984	14.2	6.9	7.2
1985	21.5	4.3	6.8
1986	32.0	8.4	6.4
1987	31.5	9.4	6.9
1988	1.0	7.1	6.6
1989	10.0	7.6	7.8
1990	11.2	7.7	6.6
1991	9.4	3.4	5.0
1992	10.6	1.2	4.7
1993	11.5	1.9	1.8
1994	8.8	1.7	3.3
1995	7.9	4.5	4.8
1996	10.5	3.1	4.0
1997	18.9	0.3	3.6
1998	8.7	0.7	4.4
1999	8.4	1.1	3.3
2000	12.2	3.2	4.2
2001	5.6	6.0	5.3
2002	-3.5	2.8	5.2
2003	0.1	2.7	6.3
2004	13.3	2.5	3.1
2005	13.1	2.5	6.0
2006	14.6	4.0	3.4
2007	15.7	2.1	4.6
2008	-6.8	4.5	4.7 *

Notes:

- The annual returns over the past 7 years have been derived from the median returns in the SuperRatings surveys for balanced portfolios and from the ChantWest multi-manager surveys for growth portfolios. SuperRatings is a member of ASFA and Warren Chant is a member of ASFA. Annual returns longer than 7 years ago have been largely derived from average returns of funds participating in various surveys.
- CPI is the consumer price index, for all groups, as published by the Australian Bureau of Statistics.
- Wage increases are those as published by the Australian Bureau of Statistics for full-time adults average weekly ordinary time earnings (AWOTE) from 1 July 1987 and for males average weekly total earnings prior to this.

* For the year to 31 March 2008

The above table shows that over the past 40 years there have been five annual negative returns as well as three annual returns of 1% or lower.

Five Year Returns

Five Years Ending 30 June	Average Fund Return (%pa)	CPI Increases (%pa)	Wage Increases (%pa)
1974	0.8	6.7	10.9
1975	2.8	9.4	14.2
1976	6.4	11.1	14.9
1977	3.9	12.4	15.3
1978	6.9	13.2	15.5
1979	13.2	12.2	13.8
1980	18.7	10.9	10.7
1981	17.8	10.2	10.7
1982	15.5	9.6	11.1
1983	17.6	9.9	11.4
1984	17.7	9.7	11.3
1985	14.8	8.4	10.7
1986	17.6	8.3	9.2
1987	24.9	8.0	7.7
1988	19.5	7.2	6.8
1989	18.6	7.3	6.9
1990	16.5	8.0	6.9
1991	12.2	7.0	6.6
1992	8.4	5.4	6.1
1993	10.5	4.3	5.2
1994	10.3	3.2	4.3
1995	9.6	2.5	3.9
1996	9.9	2.5	3.7
1997	11.5	2.3	3.5
1998	10.9	2.0	4.0
1999	10.8	1.9	4.0
2000	11.7	1.7	3.9
2001	10.7	2.2	4.2
2002	6.1	2.7	4.5
2003	4.4	3.1	4.9
2004	5.3	3.4	4.8
2005	5.5	3.3	5.2
2006	7.2	2.9	4.8
2007	11.2	2.8	4.7
2008	9.6	3.1	4.4

The above table shows that there were no negative five year returns over the measurement period, however, there was one five year period when the return was lower than 1%pa (five years to 30 June 1974).

Ten Year Returns

Ten Years Ending 30 June	Average Fund Return (%pa)	CPI Increases (%pa)	Wage Increases (%pa)
1979	6.8	9.4	12.4
1980	10.5	10.1	12.5
1981	12.0	10.6	12.7
1982	9.6	11.0	13.2
1983	12.2	11.5	13.4
1984	15.4	10.9	12.5
1985	16.7	9.7	10.7
1986	17.7	9.2	9.9
1987	20.1	8.8	9.4
1988	18.5	8.6	9.1
1989	18.1	8.5	9.1
1990	15.7	8.2	8.8
1991	14.9	7.6	7.9
1992	16.4	6.7	6.9
1993	14.9	5.8	6.0
1994	14.4	5.2	5.6
1995	13.0	5.2	5.4
1996	11.0	4.7	5.1
1997	9.9	3.8	4.8
1998	10.7	3.2	4.6
1999	10.6	2.5	4.1
2000	10.6	2.1	3.9
2001	10.3	2.4	3.9
2002	8.8	2.5	4.0
2003	7.6	2.6	4.4
2004	8.0	2.7	4.4
2005	8.5	2.5	4.5
2006	8.9	2.6	4.5
2007	8.6	2.8	4.6
2008	7.0	3.1	4.6

Fifteen Year Returns

Fifteen Years Ending 30 June	Average Fund Return (%pa)	CPI Increases (%pa)	Wage Increases (%pa)
1984	10.3	9.5	12.0
1985	11.9	9.6	11.9
1986	13.8	9.8	11.6
1987	14.5	10.0	11.3
1988	14.5	10.1	11.2
1989	16.5	9.7	10.6
1990	16.7	9.1	9.4
1991	15.9	8.5	8.8
1992	16.1	7.6	8.3
1993	15.8	7.1	7.7
1994	15.5	6.7	7.4
1995	13.6	6.3	7.1
1996	13.2	5.9	6.5
1997	14.7	5.2	5.8
1998	13.6	4.5	5.3
1999	13.2	4.1	5.1
2000	12.6	4.0	4.9
2001	10.9	3.9	4.8
2002	8.6	3.5	4.7
2003	8.6	3.2	4.7
2004	8.8	2.8	4.4
2005	8.9	2.5	4.3
2006	9.2	2.5	4.2
2007	9.6	2.6	4.2
2008	8.3	2.8	4.4

Twenty Year Returns

Twenty Years Ending 30 June	Average Fund Return (%pa)	CPI Increases (%pa)	Wage Increases (%pa)
1989	12.3	8.9	10.7
1990	13.0	9.2	10.6
1991	13.4	9.1	10.3
1992	12.9	8.8	10.0
1993	13.5	8.6	9.6
1994	14.9	8.0	9.0
1995	14.9	7.4	8.0
1996	14.3	7.0	7.5
1997	14.9	6.3	7.1
1998	14.6	5.8	6.8
1999	14.3	5.5	6.6
2000	13.1	5.1	6.3
2001	12.5	5.0	5.9
2002	12.5	4.6	5.4
2003	11.2	4.2	5.2
2004	11.2	3.9	5.0
2005	10.8	3.9	5.0
2006	10.0	3.6	4.8
2007	9.3	3.3	4.7
2008	8.8	3.2	4.6