The Changing Retirement Landscape – an Australian Fund's experience

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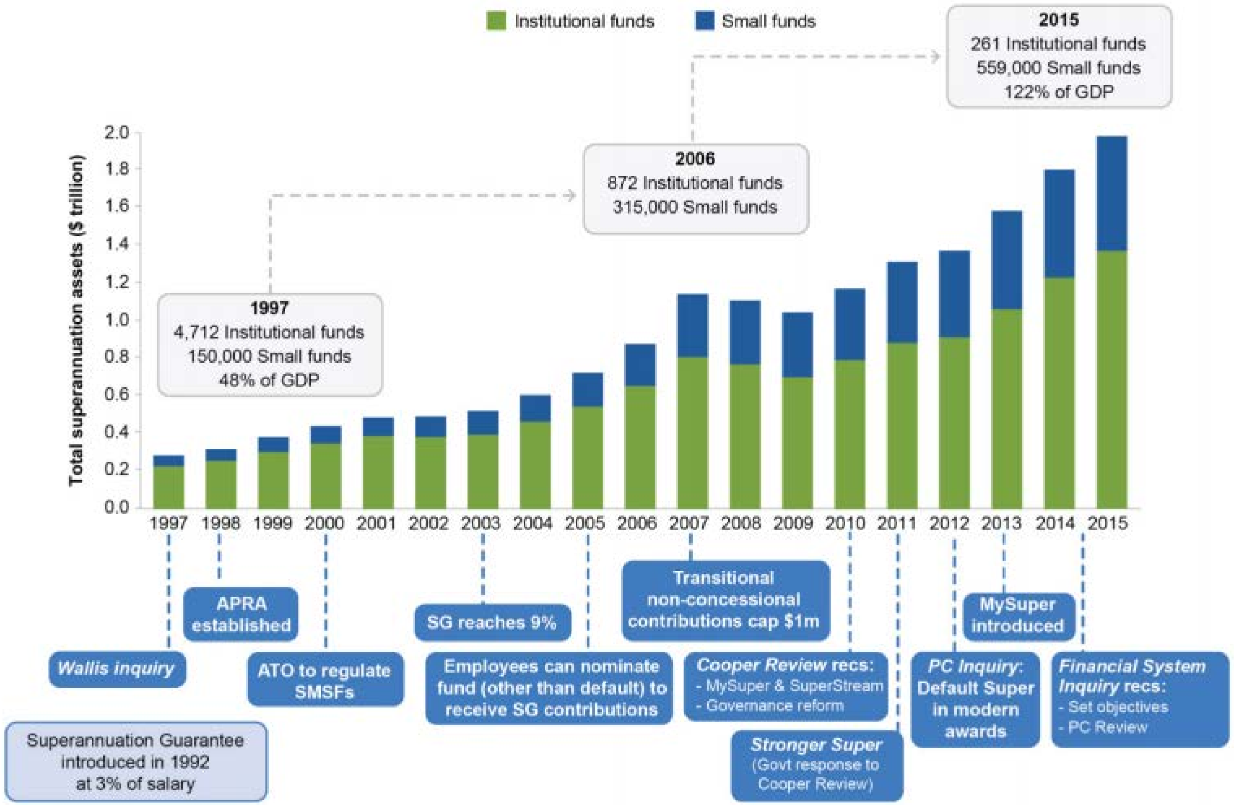
HOSTPLUS

Agenda

- On overview of Australia's retirement income policy re mandated contributions (accumulation phase)
- Today's competitive superannuation fund landscape
- Hostplus – one fund's journey to date
- The challenge facing Australia - the post-retirement phase
- How Hostplus is addressing our future-state opportunities and challenges

Key milestones – Australian Super System



Source: Productivity Commission 2016, Superannuation Efficiency and Competitiveness: Issues Paper,

1 July	Minimum contribution percentage[13][14]
1992	3 / 4*
1993	3 / 5*
1994	4 / 5*
1995	5 / 6*
1996	6
1998	7
2000	8
2002	9
2013	9.25
2014	9.5
2021	10
2022	10.5
2023	11
2024	11.5
2025	12

The ratcheting-up of the % of Super Guarantee has been gradual…but we aren't there yet…

…and its arguable this pathway is still too little too slowly.

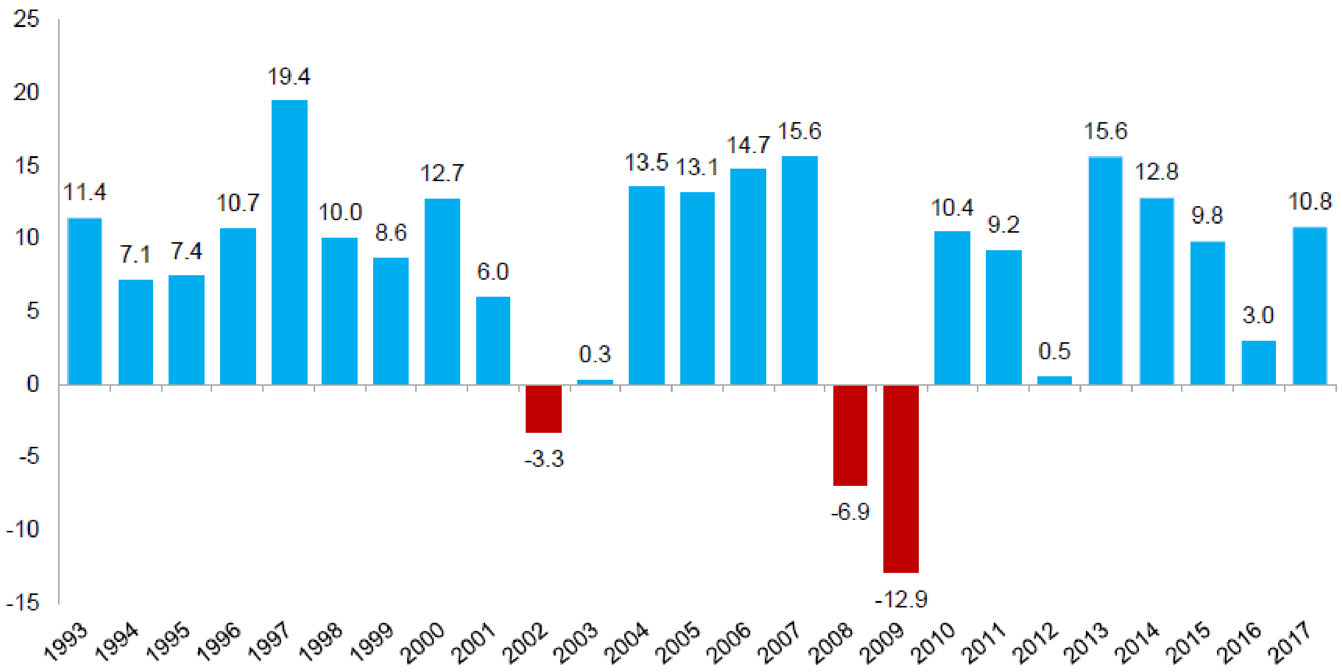
Types of Super Funds in Australia

- The dominant players and fund types:
  - Retail Funds
  - Industry Funds
  - Self-Managed
- Other fund structures include:
  - Public sector (DB /DC)
  - Corporate (DB/DC)
- Generally, employees can elect to opt-out of an employer's selected MySuper default for another fund but that employee-selected fund must still be a MySuper licenced fund to be able to receive these SG payments.

Type of fund	Total assets ($billion)	No. of funds	No. of accts (June 16)
Corporate	59	27	0.3 million
Industry	545	41	11.1 million
Public sector	379	37	3.5 million
Retail	588	128	13.0 million
Funds with less than 5 members	703	598,599	1.1 million
Balance of statutory funds	55		
Total	**2,324**		**29.0 million**

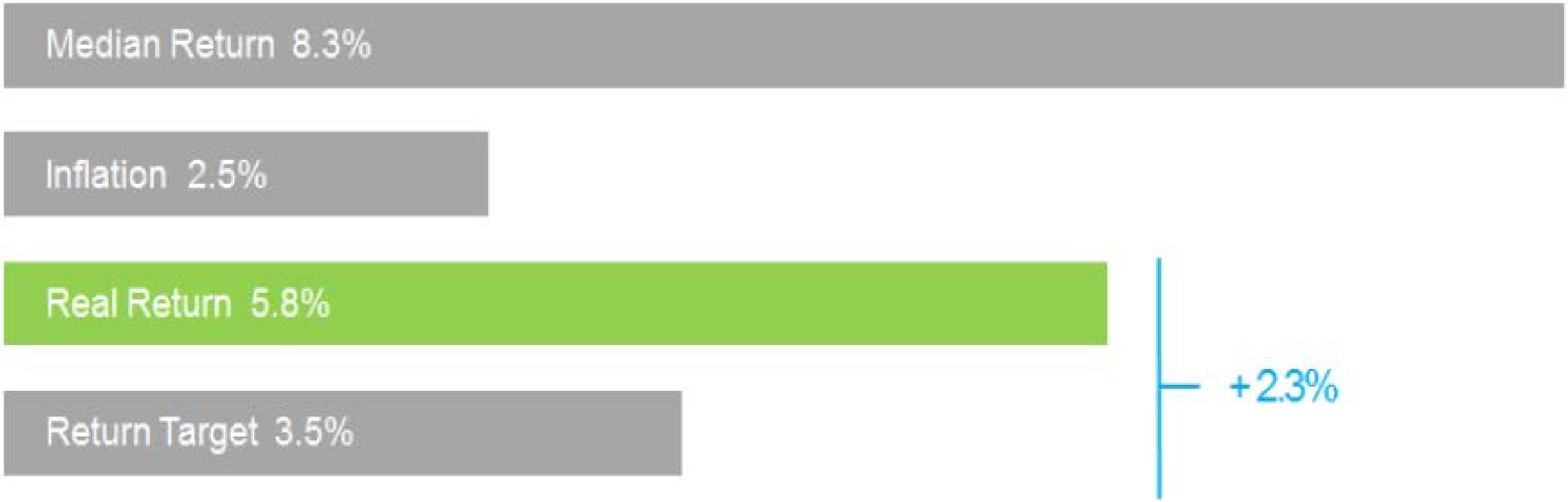
Source: APRA Statistics – June quarter 2017 and APRA annual statistics for no. of accounts

Growth Funds – Financial Year Returns (%)



Source: Chant West

Returns since 1992 – to June 2017 (% pa)



Source: Chant West

MySuper – The Minimum Default Standard

- MySuper has replaced most existing default accounts offered by super funds
- People who don't choose a super fund on joining an employer or receiving qualifying Super Guarantee contributions must have these paid into the employer's selected MySuper account
- MySuper accounts generally offer:
  - Lower fees (there are restrictions on the type of fees charged and passive investments often used to keep investment fees down)
  - Simply structured, with minimum viable product features and restrictions on "bells 'n whistles"
  - A Single or life stage investment option as default and modest investment menu at best
  - Min. prescribed level of Life insurance on opt-out basis

MySuper is only offered for accumulation funds, not for DB funds and not pension phase.

Hostplus

- Hostplus was established in 1987 and is today the largest national superannuation fund predominately focused on and a dedicated supporter of the hospitality, tourism, recreation and sports sectors in Australia.
- As an industry super fund (occupational-based master trust) our focus is on our members and employers, not shareholders.
- Our mission is to make superannuation easier for our members and their employers and maximise net returns on members super investments.

Hostplus snapshot as at 31 August 2017

Members

Over

1.1 million

Active Employers

Over

137,000

Funds under management

Over

$28.8B

Hostplus' successful investment philosophy

- We take a long-term view and approach to investing with a focus on building a solid foundation for our members future.
- Our actively managed Balanced default investment option, represents our "best ideas" in investing and aims to achieve competitive, long-term net investment returns for members.
- We also provide our members with 21 other well constructed and managed investment options to allow members the flexibility and freedom to make the investment choices that best suit their individual needs and objectives.

Hostplus' SAA is different to the pack and tailored to leverage our distinctive advantages

Asset allocation (funds with more than four members)

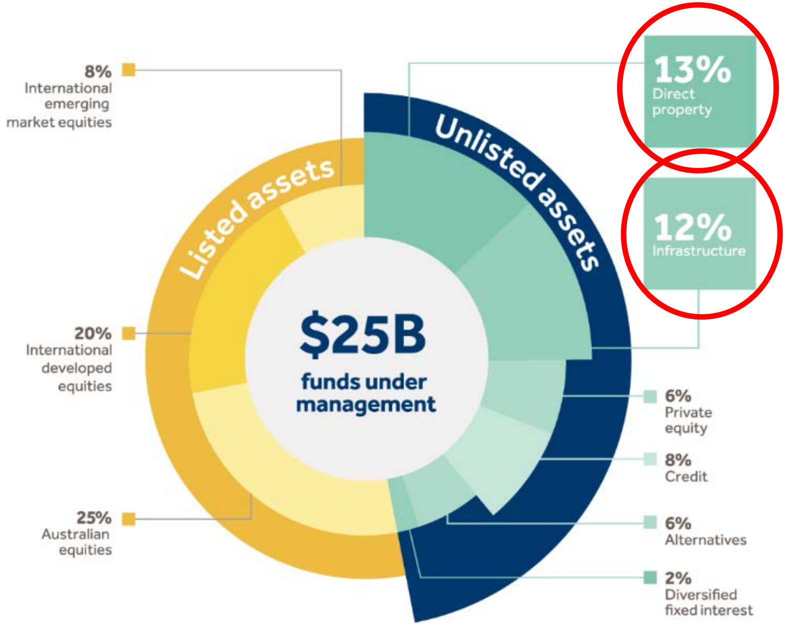
Asset class	Amount ($billion)	%
Cash	190	12
Australian fixed interest	205	13
International fixed interest	116	8
Australian listed shares	351	23
Listed property	48	3
Unlisted property	78	5
International shares	353	23
Infrastructure	77	5
Hedge funds	26	2
Unlisted equity	61	4
Other	29	2
Total	**1,539**	**100**

Source: APRA June quarter 2017.

MySuper funds

Characteristics	Amount ($billion)	%
Cash	41	7
Australian fixed interest	76	13
International fixed interest	42	7
Australian listed shares	125	21
Listed property	12	2
Unlisted property	40	7
International shares	160	27
Infrastructure	43	7
Hedge funds	0	0
Unlisted equity	29	5
Other	20	4
	595	**100**

Source: APRA June quarter 2017.
*Number of MySuper products: 111, 31 lifecycle.



Our default Balanced Option has consistently delivered market-leading net returns

Year	Ranking	Return
1 Year to 30 June 2017	**1**	**13.20%**
3 Years to 30 June 2017	**1**	9.68% p.a.
5 Years to 30 June 2017	**1**	11.76% p.a.
7 Years to 30 June 2017	**1**	9.92% p.a.
10 Years to 30 June 2017	=3	5.79% p.a.

(Source: SuperRatings Fund Crediting Rate Survey - SR50, 19 July 2017).

Post Retirement – Our Unfinished Symphony

- Super Guarantee has been running for 25 years, but little focus or policy / product development for retirement-side of the equation
- 2014 Financial System Review belled the cat – again, like in the late 80s – early 90s with accumulation, doing nothing isn't an option re retirement
- "MyRetirement" framework is under construction now and MySuper funds will be required to have a comprehensive solution for their retirees, or else convince our regulator why not

Issues we're seeking to solve

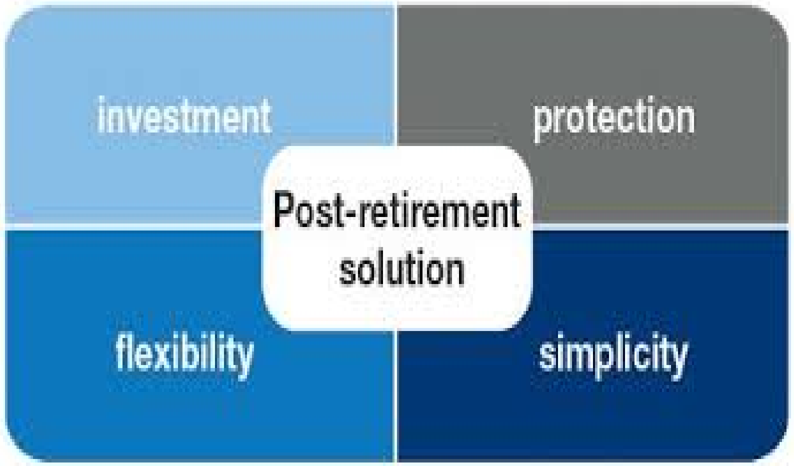
Main issues for retirees are:

- Market volatility impact on investment returns (*sequencing risk*);
- Inflation protection (*inflation risk*); and,
- … and then later on, outliving their savings (*longevity risk*).

Solutions must also be: *flexible* and *simple (both to understand and administer.*

But problem is that most retirees:

- eschew market volatility and hence "underinvest" during retirement
- are spooked into locking in expensive, low-return, life annuities from "solutions providers"
- Can't easily access risk pooling



Why the current options all fail

- **Opportunity costs**: Growth assets outperform over longer timeframes, and even 65 year olds can live for a long time
- **Complexity**: There are too many choices, not enough guidance and advice and no benchmarks
- **No risk pooling**: individuals are self-insuring, which is sub-optimal
- **Pension reliance**: Government is trying to reduce costs by making super 'work harder' and up the Age Pension qualifications, but not make pooled risk and annuity products 'sexy' again

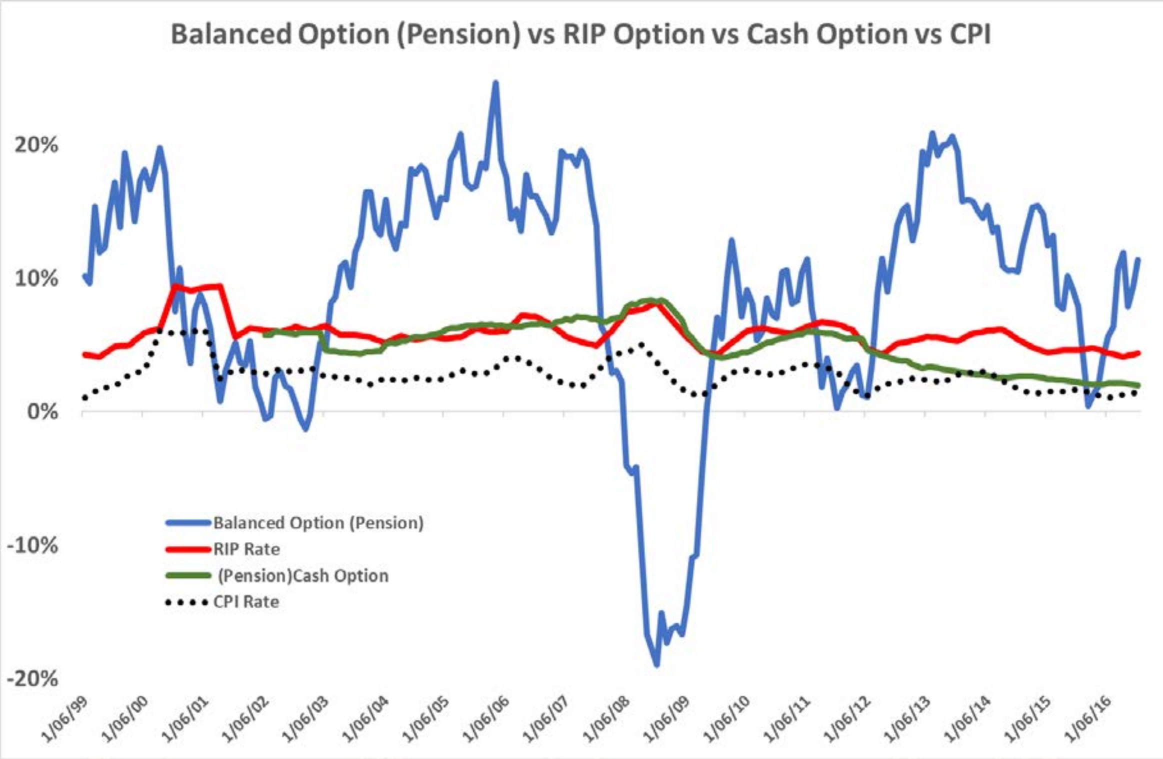
Principle / KRA	Lump Sum	ABP – Cash	ABP – Other	Annuity
Simple	✓✓	✓	✓	×
Flexible	✓✓	✓	~	×
Reduce Sequencing Risk	✓	✓	×	✓
Reduce Longevity Risk	××	×	✓	~

A proposed solution for our members

A post-retirement, account-based, investment option that credits CPI + 3%p.a.

- *How would this work?*
  - members are invested in our (untaxed) default Balanced Option… but are promised and paid CPI + 3% p.a. irrespective of the actual performance of the Balanced Option
  - members stay invested in the Balanced Option, but pay retired members the difference b/w what the default Balance Fund earns, and CPI + 3%.
- *Premise and modelling:*
  - there is $30 in Accumulation division for every $1 in Retirement division of the Fund
  - BalP <u>should</u> out-earn CPI+3% over time … but not guaranteed to do so EVERY time
  - The Balanced Option can bear more volatility than the current 5.5%.

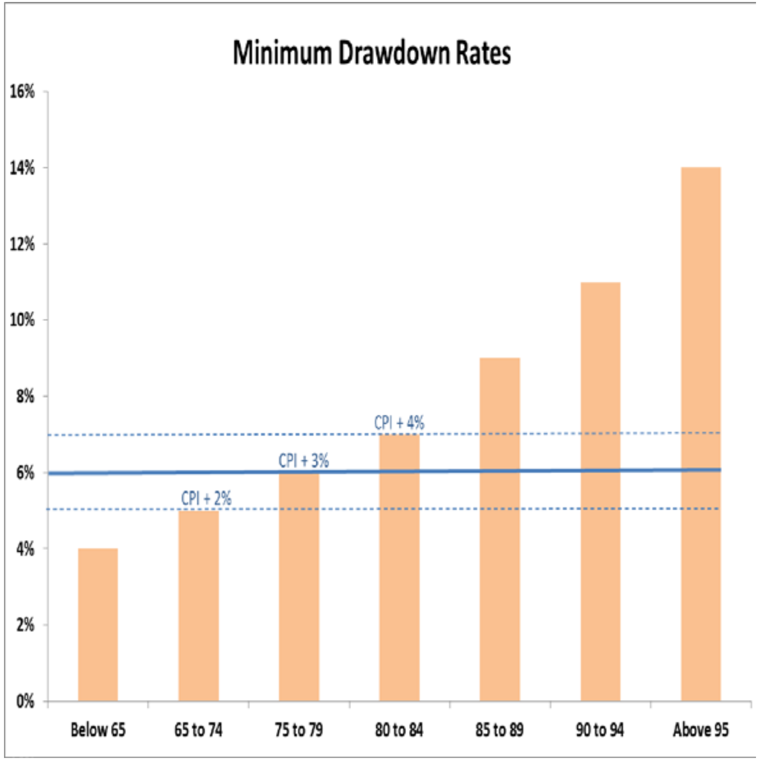
Which would a retiree rather have?



- Guaranteed certainty…market volatility, or a better risk-adjusted return over the long term?

What is our product solution?

- A "guaranteed" CPI-based rate of return. In terms of the (likely) CIPR Requirements, it would have:
  - A guaranteed income which minimises (actually removes) sequencing risk;
  - Constant real income for life: (i.e. manages longevity risk and meets inflation)
  - Flexibility at any time to access a lump sum or leave a bequest
- Modelling indicates that at CPI+3% p.a. retirees could utilise minimum drawdowns to age 80+ and still maintain their lump sum (no principal loss)



Assumes CPI = 3%

Summary

- Australia is now some 25 years into its journey towards its universal retirement income objectives
- We got a great foundation, but a lot more still to do
- Focus now to shift to the decumulation / retirement phase
- These challenges are borderless, international and don't discriminate
- No one's got all the answers
- GOOD LUCK!