

Differential Treatment by UniSuper between its accumulation and defined benefit members

I submit that UniSuper has provided a superior level of service to members on the defined benefit plan vis those on an accumulation plan.

The facts in support of the above are provided next.

Returns on investment earned by members on the defined benefit plan (DB) as reported in the attached August 2016 UniSuper 'Spotlight on investments' pamphlet for 2015-16 financial year was 11.3% and that for the 5 years to 2015-16 was 11.9 percent per annum.

The returns to investment by members on the accumulation plan (AP) for 2015-16, in contrast, varied from 3.0 percent for the 'High Growth' portfolio to 7.6% for 'Capital Stable'. The returns to 5 years to 2015-16 for AP members ranged from 10.1 percent per annum for the 'High Growth' portfolio to 7.5 percent per annum for 'Capital Stable'.

The facts are that returns on investment for members on DB plan have consistently outperformed the returns on the best portfolio of investments offered to those on AP. This difference in rates of return to investment between DB and AP members raises three questions that need to be addressed.

- (i) The consistently superior returns on investments for DB members vis their AP counterparts warrants an explanation.
- (ii) Can AP plan members be offered the same portfolio of investments as their default option as is currently being offered to their DB counterparts?
- (iii) Is there a difference in the fee charged by UniSuper for DB versus AP members? That is, is the difference in the quality of services provided reflective of the difference in fee charged to the two groups of members?

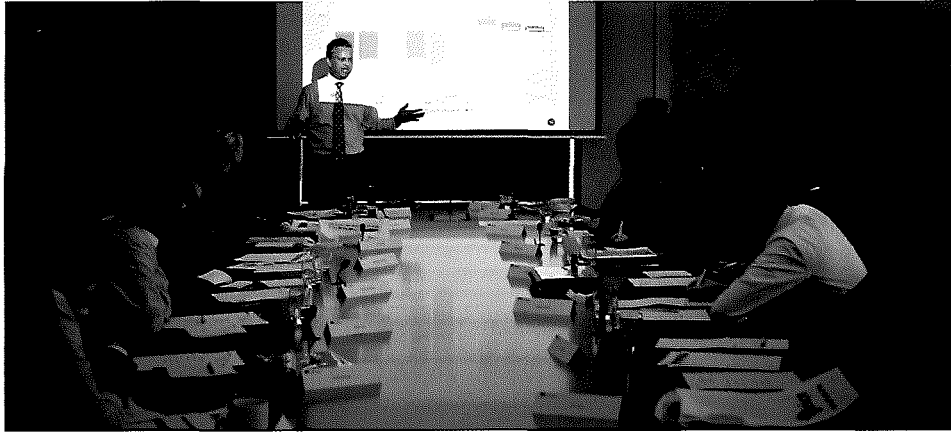
It is also important to note that UniSuper has greater responsibility to fund losses accruing to members on the DB plan given that their benefits are predetermined. The AP members in contrast bear the full risk of any movements in the market. In short, UniSuper has an incentive to provide greater returns to its DB portfolio compared to that for the AP constituents. But doing so may constitute discriminatory practice.

I have asked UniSuper for answers to the first two of the above enumerated questions but am as yet to receive a satisfactory answer. If UniSuper is delivering differential treatment to members on Defined-Benefit (DB) versus those on Accumulation Plan (AP) then I recommend the following:

- 1) Members on AP be offered an option of a portfolio of investments that is identical to that for the DB members;
- 2) The administration fee charged to DB and AP members be made uniform for the default portfolio; and,
- 3) If (1) and (2) are not feasible then UniSuper be broken into two parts with each serving a different clientele so that the benefits of competition are realized by the whole membership.

Satish Chand

Canberra
ACT 2604.



Talking institutional investing on-campus

Since 2013, we have been running an in-house designed program to provide finance students with valuable exposure to the real-world of institutional investing.

A practical guide to institutional investing is a one-day workshop that helps high-achieving students interested in investing put theory into practice—under the guidance of UniSuper's most senior investment professionals.

As the super fund for the higher education and research sector, we're passionate about partnering with universities to complement theory with the applied knowledge and real world expertise of our team.

Students have the opportunity to learn from and network with UniSuper's key investment experts—including our Chief Investment Officer John Pearce—as well as developing their understanding of how funds are invested and how asset classes are managed.

We're pleased that the program consistently receives overwhelmingly positive feedback from participating students. Having delivered workshops at a number of universities, our team continues to balance their day-to-day responsibilities with their commitment to delivering the program at other universities across Australia into the future.

Learn more about investments at UniSuper at unisuper.com.au/investments.

This is not intended to be an endorsement of any of the options or listed securities named above for inclusion in personal portfolios. The above material reflects UniSuper's view at a particular point in time having regard to factors specific to UniSuper and its overall investment objectives and strategies. Past performance is not an indicator of future performance. This information is of a general nature only and may include general advice. It has been prepared without taking into account your individual objectives, financial situation or needs. UniSuper's investment strategies will not necessarily be appropriate for other investors. Before making any decision in relation to your UniSuper membership, you should consider your personal circumstances, the relevant product disclosure statement for your membership category and whether to consult a licensed financial adviser. This information is current as at 20 July 2016.

UNISS01 0716



AUGUST 2016

Spotlight on investments

Market movements in any given year are driven by events that might look unique on the surface. It's fair to say that 2015-16 had its share of these 'unique' events, but digging a little deeper, we see an extension of themes that can be said to have characterised the 'post-Global Financial Crisis (GFC) era'.

The post-GFC themes we've observed include global share markets tending to overreact to negative surprises, the demand for bonds driven by seemingly irresistible forces (risk aversion, demographics, central bank policy and falling commodity prices), and yields on shares (and property) being persistently higher than bonds.

How the year began

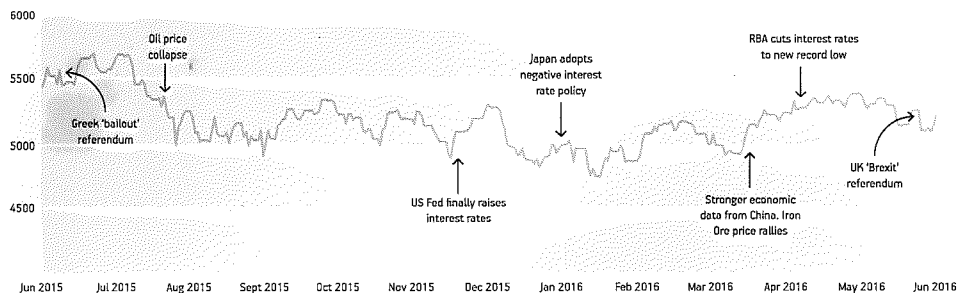
The financial year opened with hopes that the United States (US) was going to lead the world's conduct on monetary policy, moving towards some semblance of normality. Rate tightening looked likely in September, when another Greek debt bailout was agreed and Europe no longer dominated front page news. However, the calm was then shattered by collapsing commodity prices, seeing oil, coal and iron ore falling around 45%, 17% and 30% respectively in a matter of months.

Not surprisingly, the energy and materials sectors were hardest hit. Banks were also heavily sold as investors factored in a wave of loan defaults. The Australian market—with its large exposure to these sectors—was impacted heavily as shown in the graph on page 2.

The year unfolds

The US Federal Reserve waited until December before raising interest rates by 0.25%, foreshadowing further increases, although this never eventuated. Commodity prices remained weak and volatile, before finding solid footing again in February. On top of weak commodity prices, Japan's central bank surprised the market by cutting rates to negative territory, hampering any chance of moving back to 'normality'. The Reserve Bank of Australia responded to the commodity price fall and a stubbornly strong currency by cutting rates in May to 1.75%. Volatile share markets and relentless falls in bond yields received a further catalyst in late June when Britain's exit from the European Union ('Brexit') was announced. The financial year ended with more than \$10 trillion in global bonds offering negative yields. At the time of writing, the market has seemingly brushed Brexit aside, and following a strong US employment report, talk has once again turned to a rate rise before the end of the 2016 calendar year. It's hard not to have a sense of déjà vu, and we suspect the post-GFC themes discussed earlier will prevail for some time.

SGP/ASX 200 INDEX OVER PAST 12 MONTHS



Our investment performance

The table below shows selected diversified options. With close to 100% of its portfolio allocated to 'growth' assets, the High Growth option is considered our highest risk option. At the opposite end sits Capital Stable, with a 70% allocation to 'defensive' assets. The Balanced option—our default option—sits somewhere in between, with about 70% of its portfolio allocated to growth assets.

OUR INVESTMENT PERFORMANCE

	High Growth	Balanced	Capital Stable
1 year %	3.0	5.9	7.6
SuperRatings ranking	16/76	4/188	1/134
3 years (% p.a.)	10.8	10.2	7.7
SuperRatings ranking	8/71	2/171	1/124
5 Years (% p.a.)	10.1	9.6	7.5
SuperRatings ranking	9/70	2/160	1/110

Returns are for periods to 30 June 2016. Past performance is not an indication of future performance. Returns relate to our Accumulation (not Pension) investment options and are published after fund taxes and investment expenses, other than account-based fees. SuperRatings data based on SuperRatings Fund Crediting Rate Survey for periods ending 30 June 2016, published on 20 July 2016 and does not take into account any subsequent revisions or corrections made by SuperRatings.

A closer look

With a large allocation to defensive assets such as bonds, the Capital Stable option was well-placed to benefit from the continued fall in bond yields (and rise in bond prices). Over the financial year it was the second-strongest performer among our diversified options (Conservative Balanced being the strongest performer). That said, it's important to remember that super is generally a long-term investment. Over the longer term members invested in higher risk options have generally been rewarded, with our High Growth option recording the highest return since the GFC.

In the context of generally poor-performing global share markets (the MSCI World Index was negative 2.7% for the year, in local currency terms), it was pleasing to see our Balanced (Accumulation) option returning 5.9% for the year, following six years of double-digit returns (on average). This put us well within the top quartile of all surveyed balanced funds across the industry.*

* Based on the SuperRatings Fund Crediting Rate Survey for periods ending 30 June 2016 of all super funds with Balanced options within a 60%-76% growth asset range, which took part in the survey published on 20 July 2016. The SuperRatings data does not take into account any subsequent revisions or corrections made by SuperRatings. At the time of preparation, UniSuper was not aware of any revisions or corrections which would be materially adverse to members.

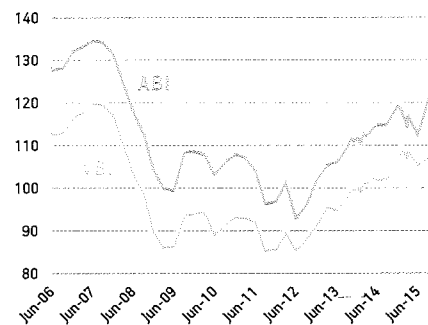
One driver of this strong return has been the performance of our key holdings in listed property and infrastructure, with a number of these investments hitting record highs in an otherwise flat market. These include Transurban (35%), Sydney Airport (45%), Duet (22%), APA (17%), GPT (32%) and Scentre (38%). UniSuper is the largest shareholder in all of these companies with the exception of Scentre, where we are one of its top three shareholders.

Defined Benefit Division (DBD) investment update

Two measures are used to regularly check the DBD's financial position; the 'Vested Benefits Index' (VBI) and 'Accrued Benefits Index' (ABI). Both of these measures are designed to measure the DBD's capacity to pay members' benefits.

At the time of writing, financial year estimates were not yet available. However, we're confident that both the ABI and VBI will sit comfortably above 100, indicating a healthy surplus position.

Movement in the VBI and ABI over the past decade



SOURCE: UniSuper

The steady improvement in the DBD's funding level can be attributed to recovering investment markets, as well as our DBD investment strategy which has benefited from large overweight positions to the strongest-performing market sectors.

The DBD's portfolio is dominated by large investments in 'fortress assets' including the listed infrastructure and AREIT stocks mentioned earlier. The DBD portfolio returned 11.3% over the 2015-16 financial year and 11.9% p.a. over the past five years. To put this in context, although the DBD is not included in any survey, the portfolio's return over five years to 30 June 2016 is higher than the reported return of all diversified fund options included in SuperRatings' surveys.

The health of our DBD stands in sharp contrast to many pension schemes worldwide. Milliman¹ tracks the 100 largest corporate DB schemes in the US and estimates average funding level to be around 77% as at end May—despite the US share market outperforming the Australian market. The disparity in performance can be attributed to differing approaches to asset management; our bias has been in favour of fortress assets, and American funds have been more heavily-weighted towards bonds.

We're proud of the DBD's performance, particularly the way it withstood recent market gyrations. In an ideal world, a healthy surplus would provide the opportunity to 'de-risk' the portfolio by investing in long-term bonds, matching the profile of the DBD's liabilities. However, the yield offered in bond markets is not yet at a point where we believe this is the best choice. We'll continue to carefully monitor and adjust the portfolio where we see the best and most prudent opportunities for sustaining the DBD.

¹ Milliman is a global provider of actuarial and related products and services to a range of clients including business, financial, government, union, education, and non-profit organizations. www.milliman.com