AustralianSuper builds $70m war chest

March 7, 2019

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The last few years have seen AustralianSuper dominate the pensions landscape in Australia, topping the charts in terms of net flows year after year. The fund has never been afraid of making some big decisions (think of the internalisation of investment that has occurred over the last few years) and 2019 is set to be no different. The nation's largest superannuation fund recently increased administration fees by 50% to $117 per annum.

To say that this goes against the grain is an understatement – in the last few months alone Vision Super and MTAA have *reduced their fees*, and neither of those funds has anything like the scale of AustralianSuper. Even the banks have been coming to the party (BT with BT Open and MLC with reductions for MLC Wrap).

Of course, AustralianSuper hasn't increased its fee since 2009, and given its flat fee structure, the fee doesn't increase naturally through FUM growth (as it does for most other funds, which have a partially variable admin fee). Nevertheless, such a big shift begs the question:

What is AustralianSuper planning to do with an extra $70m+ per year?

According to their communications with members, the additional funds will be put towards the development of products and services, benefits for members and the digital proposition. Based on the fund's submission to the Royal Commission, the additional revenue will represent almost a 3 fold increase in their 'cost to grow'. That is, the cost of improving member services and experience will increase from $46m in 2017 to around $120m per year.

Knowing that the largest superannuation fund in the country has just armed itself for significant investment in improving its proposition on an ongoing basis, competitors should be seriously asking themselves how they will compete. If AustralianSuper has just fired the first salvo in an anti-price war, each fund needs to be able to clearly articulate its war footing.

Proposition vs price

The battle between retail and industry super funds has been fought on costs (flowing through to investment returns) and even if retail funds haven't declared their loss, it's clear the industry funds are winning hand over fist. This latest move by AustralianSuper shows a shift in direction. Such a large investment in *proposition* cannot be achieved whilst maintaining a *cost leadership* position.

Fast forward a few years and it appears the fund's intention to be the unequivocally the *best* fund in the market, not the cheapest. This shift – and the size of the pending investment – requires an immediate strategic response from other funds, which face two options.

Option 1 is to raise fees, to invest, to improve your proposition to match or better the biggest funds. This will suit a small number of funds with sufficient scale to raise significant sums from fee increases to be able to match AustralianSuper's improving proposition (if not dollar for dollar, then perhaps smarter). This requires a bet against the strategic assumption that there is a genuine first mover (scale) advantage in rapidly improving the proposition that means this is ultimately a 'winner takes it all' market.

Option 2 is to reduce fees. Not by 5%, but drastically. In reality, given the average fund spends 2/3 of its revenues on investments this will require a shift to a primarily passive portfolio (it's difficult to see where else significant cost savings could come from). This requires a strategic bet that *price drives selection* – and if it's any comfort that holds true in most transparent markets we operate in, in most segments, globally. There are examples of it being true here in Australia, too – just look at the success of Hostplus in recent years (boosted by the followers of the Barefoot Investor), and ING Living Super (when it was 'free').

The time to decide is now. Where strength in employer relationships or adviser distribution have been key success factors in the past, those relationships are breaking down and funds must search for an alternative point of differentiation, an alternative reason for being. It is difficult to imagine a fund without a market-leading proposition, or an eye-wateringly low price, will still be relevant five years from now.

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