

Topic 4: Limitations with typical benchmarks for SMSFs

How is your SMSF going? Good...? How do you know?

If you want to benchmark your SMSF performance over the past year, you firstly need to know what your total fund return was, using a Time Weighted Return (TWR) method. But then what do you compare it against?

The S&P / ASX 200 Index in the news?

Perhaps you listen to the TV or read the paper and see how much the ASX 200 has gone up, and compare your fund to that.

But the ASX 200 in the news is just a price movement. You would also have earned dividends. You have probably also made contributions or drawn pension payments, so you have not had a consistent amount invested throughout the period. How do you benchmark that?

Then there's the fact that only (say) 30% of your fund is in shares at the moment. The rest is in defensive assets. How do you benchmark your total fund performance? Your decision to have some defensive assets in your portfolio has had a positive or negative impact on your fund performance so you can't ignore it.

Australian Shares



Defensive assets



What about the fact that over the past 3 years you held 80% Shares / 20% Defensive assets for 2 years and 6 months, and it's only in the past 6 months that you have changed to 30% Shares / 70% Defensive. How do you benchmark your 3 year performance?

How did you decide to invest your Defensive assets anyway?

Term Deposits



Broader Fixed Interest



You may have chosen to invest your Defensive assets in Term Deposits, but you could have chosen something like Exchange Traded Funds which invest in broader fixed interest, such as corporate notes.

So in many cases the ASX200 index is not going to be a suitable benchmark for an SMSF, even if you do have access to the S&P / ASX 200 Accumulation Index, which accounts for dividends.

Model Portfolios?

Some advisers use “Model Portfolios” to benchmark their SMSF clients’ performance. Some real example are the following Morningstar ones.

1. Morningstar Multi-sector portfolios

Multi-Sector Index Asset Allocation as at 30 June 2013					
					
Asset Class %	Conservative	Moderate	Balanced	Growth	Aggressive
● Australian Shares	10.35	14.19	23.61	33.20	38.71
● International Shares	9.24	10.43	21.16	28.79	40.45
● Australian Listed Property	3.26	3.16	3.56	4.58	4.63
● International Listed Property	0.39	0.91	1.24	2.07	2.12
● Unlisted Property	0.04	0.82	1.35	1.52	1.33
● Mortgages	0.00	0.19	0.15	0.02	0.00
● Australian Fixed Interest	25.80	30.16	20.44	14.50	3.98
● International Fixed Interest	14.23	12.43	9.92	6.75	3.02
● Australian Cash	36.68	27.71	18.58	8.58	5.76

Consider the Balanced portfolio, and look how much is in International Shares. 21.16%.

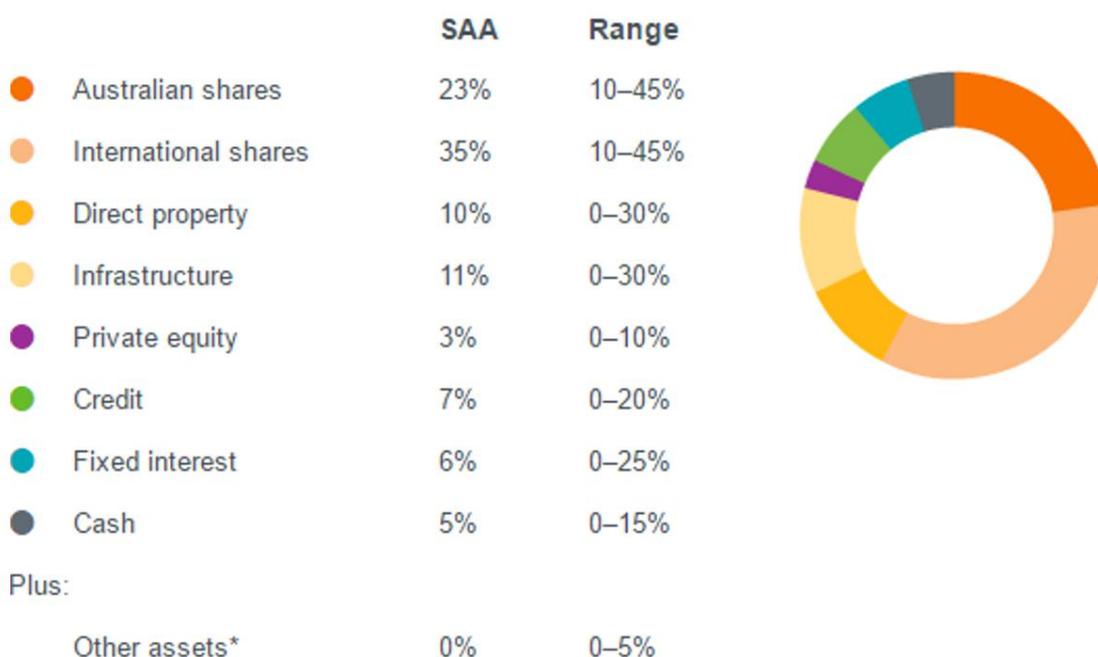
According to ATO Statistical reports, most SMSFs have a much lower exposure to international shares. This is especially so for self-directed SMSFs.

So in a year where International shares out-performed Australian shares, most SMSF trustees who used this benchmark would believe that they had under-performed over the period. In fact the real problem was more that they using an inappropriate benchmark.

This mix of assets is more typical of how a large managed fund invests, not how SMSFs invest.

An Industry Super Fund?

Some SMSF trustees may benchmark their fund against an Industry Super Fund. Consider the following example recently taken from Australian Super (Balanced fund).



This fund has 35% in International shares, as well as 11% in infrastructure and 3% in private equity.

Unless the SMSF also has a similar mix of assets, this is not a suitable benchmark for them. It will tell them the return they would have received had they been in this fund over the past year, (except for the timing and amount of contributions and pension payments) but it will not tell the SMSF trustee whether they received the return they were entitled to, given how **they** wanted to invest.

Performance Reports from administration services?

Typically, when you receive a performance report from an administrator they tell you what your return was, and how that compares to a benchmark of some kind.

Let's say you currently have 60% Growth assets / 40% Defensive assets. They will use your current asset allocation and look backwards, using something else with a 60% / 40% mix and benchmark your 3 year performance against that, just because that's the mix of assets you have at the end of the period.

But what if you had actually invested with 90% Growth / 10% Defensive for most of the past 3 years before recently changing to the 60% / 40% mix? They typically cannot give you a dynamic benchmark based on how you actually invested over the past 3 years, unless they customise it for you, which is labour-intensive and expensive, yet valuable.

The Information Gap

For all of the above reasons, it has been very hard for SMSF trustees to obtain good benchmarking information which is relevant for them.

It is not the fault of trustees, advisers or accountants. There has been a lack of good information available for them to use.

Research presented by Professor Ron Bird at the University of Technology Sydney (UTS) Investment Management Research Conference in Sydney last Friday found that improving the performance of their retirement savings fund was a key aspiration for members to adopt an SMSF, but many members were not sure whether they had actually achieved that aspiration.

“We asked our sample a series of questions about their aspirations when moving into an SMSF, and two interesting results came out of that,” Bird told the conference.

“The main aspiration for members was that they thought they could achieve better investment performance, that was the main aspiration for switching. The other main aspirations all relate to control.

“When you look at the results, people are reasonably satisfied with their investment outcomes, but it also seems that they have no grounded reason for thinking that. They have no numbers or understanding of performance, and couldn’t possibly make this judgement. The most worrying thing in the research was that we don’t have any idea about how these funds perform, and perhaps we should.”

The Rub: 4/10/2017

In fact benchmarking is a new service that accountants and advisers could be offering SMSF trustees, especially the self-directed ones, to bridge this information-gap, to empower them and help them make better decisions.

SMSF trustees need better information in this area, and professional advisers are well placed to help them.