Issue #15 September 2021

KAURI ASSET MANAGEMENT

Kauri Communiqué

Keeping you up to date with Kauri Asset Management and the Markets

Australia's worst-performing super funds - why you should take notice

Thirteen super funds have fallen short when it comes to fees and performance. Are you in one of these funds.

Monthly Portfolio Reports

Our portfolio managers take you through the main contributors and cover any changes across both the Australian and US markets.

MICHAEL SMITH
Head of Research and Senior Investment advisor

Australia's worst performing super funds - why you should take notice

Thirteen super funds have fallen short when it comes to fees and performance. Are you in one of these funds?

Last financial year was a bumper period for a number of superannuation funds, with returns dwarfing those of any recent year and marking a significant turnaround from the dour numbers posted in the 12 months prior.

However, superannuation members may be forgiven for thinking that merely achieving a double-digit return was good enough, with a number of funds all too happy to spruik a return in the mid-teen percentage range. In contrast, the best-performing super products, including our flagship Hub24 Portfolios, comfortably returned more than 20%.

That's not the end of the matter either. After the government passed recent changes to the superannuation system, it has empowered the Australian Prudential Regulation Authority (APRA), the financial watchdog, to assess the most-popular super products.

In the first annual review to take place under the new provisions, APRA has assessed the performance, adjusted for fees, of 76 MySuper options, the default accounts for those who don't nominate an investment preference.

These funds have been assessed based on the last seven years of results, compared with variable benchmarks for what APRA deems a super product should have returned according to its asset allocation and industry fees. Funds that underperform their benchmark by more than 0.5 percentage points are deemed to have failed.

The outcome of this analysis has seen APRA identify 13 super products that fall short of its test. By the end of this month, members in these products will receive a letter from their fund informing them that their superannuation product has performed "poorly", and that they may be best-served by reconsidering where their super is held.

In news that may surprise readers, not to mention, affected members, the 13 super funds identified by APRA collectively hold $56 billion in assets. These are not small funds, especially with around 1.1 million Australians being members of these funds.

Who failed the performance test?

Headlining the names that failed to stand up to the regulator's performance assessment were the Colonial First State FirstChoice Superannuation Trust and BT Super's Retirement Wrap.

These two retirement funds alone comprise nearly 800,000 Australians. In fact, we regularly on-board clients who have come from these funds. Poor performance has been something we have identified in many instances, and it's a point of concern that everyone should take into account. Even a small difference in fees and returns can have a profound impact on your super balance by the time you retire.

This is something that underperforming super funds will be required to spell out to investors, with data suggesting that "by earning 1 per cent higher net return over a 30-year period, you could be 20 per cent better off at retirement."

What's more, data from the Productivity Commission in 2019 identified that a member in the worst-performing super fund could theoretically increase their retirement savings by more than $600,000 if they rolled over into the best-performing fund.

A complete list of the 13 worst-performing super funds identified by APRA includes:

- Colonial First State FirstChoice Superannuation Trust
- BT Super Retirement Wrap (BT Super MySuper)

- Australian Catholic Superannuation and Retirement Fund - LifetimeOne
- AMG Super (AMG MySuper)
- Labour Union Co-Operative Retirement Fund (MySuper Balanced)
- Maritime Super (MySuper Investment Option)
- ASGARD Independence Plan Division Two (ASGARD Employee MySuper)
- The Victorian Independent Schools Superannuation Fund (VISSF Balanced Option - MySuper Product)
- Commonwealth Bank Group Super (Accumulate Plus Balanced)
- Boc Gases Superannuation Fund (MySuper)
- AvSuper Growth (MySuper)
- Christian Super (My Ethical Super)
- Energy Industries Superannuation Scheme-Pool A (Balanced MySuper)

Time to act

At the heart of this new campaign to call out underperforming super funds is an effort to drive consolidation within the industry that will effectively allow funds to reduce fees, and ideally, improve their performance.

Even in the short time since the changes took effect, as many as eight super products have already exited the market. The government suggests the reforms will save Australians nearly $18 billion over 10 years.

We believe the changes are long overdue, as the ability for super members to source independent information on their fund's performance has often been clouded by non-standardised timeframes and little insight into what sort of returns are a realistic goal. Importantly, this assessment will be extended to a wider range of super products from next year.

While underperforming funds will also have the opportunity to explain why their returns have significantly lagged the rest of the industry, and also outline their plans to address their underperformance, if any of these funds record two strikes in a row they will be suspended from taking on new super funds until their performance improves.

In the meantime, APRA will be keeping a watchful eye over these funds insofar as dialogue and requesting additional information, not to mention the prospect they reserve the right to mandate that funds transfer their members to another superannuation provider if deemed necessary.

Now more than ever, thanks to these reforms, the incentive is very clear for Australians to do their homework. Super members would be wise to do their research and see what other super products can make their retirement money work harder.

The key here is to look at the performance of your super fund over an established timeframe. Individual variations are somewhat par the course within the industry, although significant variances, as seen throughout last year's bumper financial period, and especially over a 5-year, 7-year or 10-year timeline should be cause for concern.

Absolute returns are one thing, but relative returns, compared with other funds, and against industry benchmarks, are fundamental. On top of that, you will also want to look at what your fund offers in terms of insurance cover and any other benefits. Even then, certain investors may prefer a specific investment mandate that aligns with their views.

If you are a member in one of Australia's worst-performing super funds, we would encourage you to reach out. We are in the position where we can help members review their investment options, and our flagship Hub24 Portfolios, which are quickly gaining traction in a modest time, have posted industry-leading returns in recent financial years. With the writing on the wall, now is not the time to be complacent.

Mike Smith
Managing Partner

MICHAEL SMITH
Head of Research and Senior Investment advisor

George Wong
Senior Financial advisor

International

International Growth Portfolio

Last month saw NAV of the Growth Portfolio increase by 2.8%, which was broadly in line with the largest stocks that make up the market. By way of comparison, the S&P 500 gained 2.9%, the Dow Jones put on 1.2%, and the Nasdaq was the standout of the bunch, climbing 4%.

Tech stocks were a key driver of our results last month, as well as the broader market. Our underperformance compared with the Nasdaq was in part due to the surge of biotech and pharma stocks throughout August, whereas the Portfolio has little exposure in this regard outside of Pfizer (PFE), which we sought to buy extra shares in.

Nonetheless, mega-tech stocks were the strongest performers for the second month running, with Apple (AAPL), Alphabet (GOOGL) and Microsoft (MSFT) all caught up amid the euphoria and positive sentiment surrounding the tech sector.

Software names like Adobe (ADBE), Atlassian (TEAM) and Palantir (PLTR) each put on a formidable showing. Atlassian and Palantir both delivered strong earnings reports in recent weeks, and that has proven a catalyst for both stocks thanks to their growth profiles.

Other notable gains came from the likes of Intuitive Surgical (ISRG) and Nvidia (NVDA), while Costco (COST) bucked the trend as one of our defensive holdings that still managed to claw out a 6% rise throughout the month.

Waning interest in payments processors Mastercard (MA) and Visa (V) weighed on the Portfolio as a reopened economy sees some shift in shopping activity back to brick-and-mortar stores. However, we still see digital payments as fundamental to the digital economy, and much of the growth for these companies might be sourced internationally.

The biggest drag on the performance of the Portfolio was Alibaba (BABA), with the Chinese e-commerce giant still feeling the effects of regulatory action. The stock may have hit a new 52-week low in August, but our conviction in the stock hasn't wavered as we feel it is significantly undervalued given the company's underlying fundamentals.

Unrealised gains across the Portfolio increased from approximately 21.7% of closing Portfolio NAV in July to 22.8% last month. With the Federal Reserve doing everything within its remit to reassure investors that interest rates won't rise any time soon, current market dynamics remain conducive to our strategy. We may add to existing holdings where opportunities present themselves, otherwise, we do not anticipate changes to our core holdings at this time.

Performance:

Index	*August Performance*	*2021 Performance*
Dow Jones	1.2%	15.5%
NASDAQ	4.0%	20.9%
S&P 500	2.9%	20.4%
Global Growth Portfolio	2.8%	17.4%

Top 10 Holdings:

Code	*Company Name*	*Weighting %*
MSFT	Microsoft	7.2%
AAPL	Apple	6.3%
GOOGL	Alphabet	5.6%
COST	Costco	5.5%
PG	P & G	4.4%
TGT	Target	4.1%
ISRG	Intuitive	4.1%
BRKB	Birkshire	3.7%
V	Visa	3.7%
HD	Home Depot	3.7%

George Wong
Senior Financial advisor

MICHAEL SMITH
Head of Research and
Senior Investment advisor

Hub 24 - Conservative

Conservative Portfolio

NAV for the Conservative Portfolio eased by 0.23% last month, which lagged the 1.9% gain for the benchmark ASX 200 index.

Despite the headline variance, much of the underperformance can be attributed to the timing of our dividend stocks trading ex-dividend, as well as some deterioration in the iron ore names that have underpinned gains across recent months.

Some of the stocks that delivered yield for the Conservative Portfolio last month included Commonwealth Bank (CBA), KKR Credit Fund (KKC), Newcrest Mining (NCM), Rio Tinto (RIO) and Telstra (TLS).

Two of the above names, in Newcrest Mining (NCM) and Rio Tinto (RIO), were also the biggest drags on the Portfolio in terms of capital growth, with unfavourable commodity movements proving a headwind. The same issue extended to BHP (BHP), with iron ore prices entering bear market territory.

The performance of Hearts and Minds (HM1), which shed more than 5%, was disappointing, however, not only have we seen it retrace some of these losses in September thus far, but the stock provides access to a suite of high-conviction investment choices that have the potential to offer income and modest growth. The stock was also one of our best-performers in July, so we should not feel compelled to act after a modest pull-back across a short time-frame.

Elsewhere, the Portfolio's winners last month were characterised by defensive names that have often been the driving force of the broader stock market. This included the likes of Macquarie Group (MQG), which hit an all-time high, as well as CSL (CSL), Woolworths (WOW), and the ASX (ASX), which were all buoyed by strong earnings results last month.

We made some adjustments to the weight of assets within the Portfolio last month, with the largest change being a decision to sell our holdings in the Vanguard Australian Government Bond Index ETF (VGB). Although we previously flagged bond exposure as an integral part of our Conservative Portfolio, we have instead sought to gain exposure to this by diverting additional capital into the PIMCO Global Bond Fund and PIMCO Global Credit Fund.

Following these changes, we feel the balance of the Portfolio now better reflects our desired asset weightings. However, we may make changes to individual positions in the Portfolio, such as reducing our exposure to mining stocks, should conditions warrant an adjustment.

Performance:

Index	*August Performance*	*2021 Performance*
ASX 200	1.9%	14.4%
ALLORDS	2.1%	14.2%
Conservative Portfolio	-0.23%	7.7%

Top 10 Holdings:

Code	*Company Name*	*Weighting %*
NABPD	NAB Note	7.3%
MQGPC	Mac Note	7.3%
CBAPD	CBA Note	6.9%
CBAPH	CBA Note	6.9%
FUND	Pim Gov Bond	4.5%
CBA	Comm Bank	4.5%
KKC	KKR Credit	4.4%
HM1	Hearts & M	4.4%
BHP	BHP Group	3.5%
FUND	Pim Credit	3.5%

Hub 24 - Balanced

Performance:

Index	August Performance	2021 Performance
ASX 200	1.9%	14.4%
ALLORDS	2.1%	14.2%
Balanced Portfolio	-0.4%	5.5%

Top 10 Holdings:

Code	Company Name	Weighting %
MQGPC	Mac Note	4.9%
CBA	Comm Bank	4.8%
BHP	BHP Group	4.5%
HYGG	Hyperion	4.5%
KKC	KKR credit	4.3%
FANG	ETF	4.3%
CBAPH	Comm Note	3.9%
WOW	Wollies	3.7%
NABPD	NAB Note	3.2%
WBCPJ	WBC Note	3.2%

Balanced Portfolio

The NAV of the Balanced Portfolio retreated by 0.4% in August, trailing the ASX 200, which advanced 1.9% throughout the month to reach a series of new all-time highs.

Underperformance was due to the Portfolio's iron ore exposure, including names such as BHP (BHP), Rio Tinto (RIO) and Fortescue Metals Group (FMG), which each fell between 10-15%.

Iron ore prices have plummeted over recent weeks as the Chinese economy shows signs of slowing and its government seeks to curb steel output. Production volumes have been wound back quite notably, which has in turn diminished demand for iron ore, a key ingredient required to make steel.

Even then, it is our view the extent of the drop in iron ore stocks has been overdone. While iron ore prices were always due to correct and return to more 'normalised' levels, each of the major miners is still making significant margins at these lower prices, and more than enough to continue paying lofty dividends.

We made the decision to exit the Tribeca Global Natural Resources Fund (TGF), which was another drag on the Portfolio. This was driven by our preference to reduce exposure to commodities so that we could divert more capital towards international assets, namely in the tech sector. To cater to this, we added units in both the Betashares Nasdaq 100 ETF (NDQ) and ETFS FANG+ ETF (FANG) to the Portfolio.

In terms of winners, Afterpay (APT) was the biggest contributor to the Portfolio, and one that we capitalised upon and took most of our profits off the table. The company received a takeover bid from US payments giant Square at the start of the month, helping it soar more than 37%.

To help us gain more exposure to international shares, we also sold out of stocks we feel have reached fair value, including Santos (STO), Race Oncology (RAC), REA Group (REA) and ResMed (RMD). In their place we added units in the Hyperion Global Growth Fund, as well as the VanEck MSCI International Quality ETF (QUAL) and Vanguard US Total Market Shares Index ETF (VTS).

August was very much a month of transition for the Portfolio. We fine-tuned our holdings to better reflect our investment strategy, and in the process, we believe we have positioned the Portfolio for risk-adjusted growth thanks to greater exposure to international equities.

Performance:

Index	August Performance	2021 Performance
ASX 200	1.9%	14.4%
ALLORDS	2.1%	14.2%
Growth Portfolio	-1.0%	6.0%

Top 10 Holdings:

Code	Company Name	Weighting %
MQGPC	Mac Note	5.0%
FANG	ETF	5.0%
CBA	Comm Bank	4.8%
HYGG	Hyperion	4.6%
HM1	H & M	4.6%
BHP	BHP Group	4.1%
XRO	Xero	3.7%
CSL	CSL Limited	3.5%
CBAPE	CBA Note	3.2%
RIO	Rio Tinto	3.1%

Hub 24 - Growth

Growth Portfolio

After fees, the Growth Portfolio recorded a drop in NAV of 1% last month. In comparison, the benchmark ASX index climbed 1.9%, driven by a number of companies that excelled throughout the reporting season.

The best-performing names in the Growth Portfolio mirrored those of the Balanced Portfolio, with Afterpay (APT) leading the way ahead of the likes of CSL (CSL), Aristocrat Leisure (ALL), and also Xero (XRO).

Whereas Afterpay's gains were driven by its $39 billion takeover bid, CSL (CSL) was the beneficiary of a strong earnings report.

Xero (XRO) rose 8.2% last month as the cloud-based accounting platform launched the Xero App Store across the ANZ and UK markets. We believe the opportunities for monetisation provide a strong runway for the company to keep growing. Similarly, Aristocrat Leisure's (ALL) online gaming business provides a stream of revenue that can withstand the impact of COVID restrictions, and it has helped drive the share price to an all-time high.

As was the case with our Conservative and Balanced Portfolios, iron ore shares were the fundamental driver of last month's underperformance, alongside a slide in the share price of the Tribeca Global Natural Resources Fund (TGF). We have a higher tolerance for volatility and commodities within the Growth Portfolio, but we have sought to divert some capital into international equities.

As we believe names such as Santos (STO), Race Oncology (RAC), REA Group (REA) and ResMed (RMD) have limited upside from here, we replicated the actions of our Balanced Portfolio and sold out of these stocks, while also exiting Alliance Aviation (AQZ) and Northern Star Resources (NST).

We have taken up positions in the Hyperion Global Growth Fund, in addition to the VanEck MSCI International Quality ETF (QUAL) and Vanguard US Total Market Shares Index ETF (VTS). These funds will provide us exposure to a host of high-quality international stocks that we believe offer strong growth prospects, and the ability to drive higher levels of performance compared with local shares.

With the Federal Reserve providing clear guidance it does not plan to lift rates any time soon, and the RBA now extending the timeline of its QE program, it is our view the outlook for the market is still positive. Having repositioned towards global equities through August, we feel there is upside as our investment strategy is afforded time to play out.

KAURI ASSET MANAGEMENT

Level 20
15 Castlereagh Street
Sydney NSW

GPO Box 2348
Sydney NSW 2001
Australia

PH 02 8379 1868
E info@kauriam.com.au

www.Kauriam.com.au