BT Panorama

SMSFs – the next wave

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CORE|DATA

Contents

The self managed super fund (SMSF) sector has been through a period of immense growth since its inception, to become the largest part of the $2 trillion Australian superannuation industry today.

But what lies ahead for SMSFs? Many commentators believe the growth in SMSFs has peaked and the golden years are behind us, however while there are some logical reasons for the tapering in the growth of new funds being established, there are also some fundamental changes underway in the sector that are likely to underpin the popularity of SMSFs in the future.

The sector continues to evolve away from the traditional do-it-yourself (DIY) proposition to an advised proposition as a result of the new wave of trustees who are looking for more of a help-me-do-it approach to managing their super. Further, the digitisation of SMSF investment management and administration via platforms and other online technology increases the appeal of the sector to young, digitally-savvy Australians.

These trends are significant and broaden the SMSF opportunity for nimble financial advisers that recognise the need to adapt their business model to capture the new breed of SMSFs, making the changes necessary to tap into this growing pool of semi-autonomous investors.

Where are we headed?

SMSF net assets grew to a record $594.6 billion in the December quarter, representing nearly 30% of the total superannuation pool[1]. In the last five years, net establishments have averaged more than 25,000 a year, and there are now more than 1 million SMSF members. The total number of funds also hit a record high in the December quarter, rising to 566,735 from 540,876 at the end of December 2014.

It seems unlikely that fund numbers will decline in the near future, although there are some trends that suggest growth may not be as spectacular as it has been in the past. If we set aside the year 2007, when the spike in SMSF establishments was clearly influenced by the one-off opportunity granted to consumers to make an after-tax contribution of up to $1 million to their super fund, there are a few reasons behind the slowing of growth.

Almost 30% of SMSF members are aged 55 and over – although the proportion in this age bracket has been gradually reducing from nearly half (48.7%) in 2010. According to the ATO, while the majority of SMSFs are in accumulation phase, the number of funds entering pension phase is growing. In the last five years, the ATO has seen an 8% increase in funds moving into full pension phase and growth of 32% in SMSF members receiving benefit payments from their fund.

As SMSF members die or balances reduce due to benefit payments or poor investment performance, we may see growth in the number of wind-ups, which has an impact on net establishments. The development that is likely to have a bigger impact on the sector though is the inroads that have been made by APRA funds in affording more control to non-SMSF members with regards to their superannuation investments.

Control and flexibility remain two of the key drivers for establishing an SMSF. The fact that you can now access direct shares, exchange-traded funds and term deposits via an industry fund means there is less need to look to an alternative super structure to achieve this – particularly for members with smaller balances.

This is not to say that appetite for SMSFs has dwindled – just that the landscape is changing. The average age of members of newly established SMSFs fell under 50 years for the first time in December to 48.8, down from 54 in 2010. SMSFs are getting younger, and younger generations have different needs from both their super and their advisers, which will create new opportunities for those servicing SMSF clients. Further, five consecutive years of positive returns for the SMSF sector is likely to boost consumer confidence in the sector.

But there are also regulatory forces that will shape the future for SMSFs and their advisers. Traditionally the domain of the ATO, ASIC's footprint in the SMSF sector appears to be growing with the regulator releasing two information sheets in 2015 intended to improve the quality of advice by SMSF advisers. The 'Disclosure of risks' and 'Disclosure on costs' documents have been produced to help advisers comply with their conduct and disclosure obligations under the Corporations Act, while the regulator's surveillance activities have resulted in action taken against several SMSF auditors and administrators. The growing influence of ASIC is a natural step in the industry's maturation and is seen as a positive move in that it will improve regulation of the sector, however it also provides a timely reminder for accounting professionals with SMSF clients to get their house in order before 1 July 2016.

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1 ABS https://www.ato.gov.au/About-ATO/Research-and-statistics/In-detail/Super-statistics/SMSF/Self-managed-super-fund-statistical-report---December-2015/?anchor=SMSFannualdata#SMSFannualdata

The trustee evolution

So what does the new-age trustee look like and how are they different? Importantly, they are getting richer. For the first time, average assets per SMSF exceeded $1 million in December – growth of 23% over five years[2]. As trustee balances grow, so too does their need for professional advice around the benefits of diversification for wealth creation and preservation. The ATO's data suggests cash holdings in SMSFs have hit a record high, with cash and term deposits reaching $155.4 billion in the December quarter, up from $154.5 billion the previous quarter. This is despite the cash rate sitting at historically low levels. Cash investments now represent 26% of all SMSF assets while Australian equities account for 30%. SMSF domestic share holdings rose 6.3% to $178.4 billion, up from $167.9 billion in the September quarter. In comparison, only $1.9 billion was invested directly in overseas equities – just 1% of the amount being ploughed into local shares.

Financial advisers have a role to play in helping trustees diversify their portfolio and incorporate new and emerging investment strategies into their fund, such as capital funding opportunities or limited recourse borrowing, but the benefit goes beyond pure investment advice. Contribution and pension strategies, estate planning and tax are all areas where trustees can benefit greatly from advice from a professional. While in the past, many trustees were closed to the idea of seeking advice from an adviser in the management of their SMSF, research shows the behavioural profile of the trustee is changing, with this evolution opening the door to partnership-style relationships for advisers and trustees. In the SMSF Association Intimate with Self-Managed Superannuation Report[3], CoreData detailed the various behavioural profiles that exist within both the broader Australian population and the SMSF trustee population – controllers, coach seekers and outsourcers.

- Controllers – are interested in managing their money and finances and enjoy doing it themselves
- Coach seekers – would rather do things themselves, but need information to support their decisions or are looking for someone to help them
- Outsourcers – would rather someone else manage their money and finances and typically pass trust to third parties when it comes to financial decision-making.

2 https://www.ato.gov.au/Media-centre/Media-releases/ATO-releases-latest-SMSF-statistics/
3 2015 Intimate with Self-managed Superannuation Report

Trustees becoming less personally involved

The early adopters wanted complete control of their superannuation and established an SMSF as a DIY alternative to APRA fund membership – ultimately driven by a desire for greater control and flexibility in their investment strategy. The 2015 Intimate with Self-managed Superannuation Report found trustees are becoming less personally involved in tasks related to their SMSF and relying more on their advisers to manage various aspects of the fund as demonstrated in Figure 1.

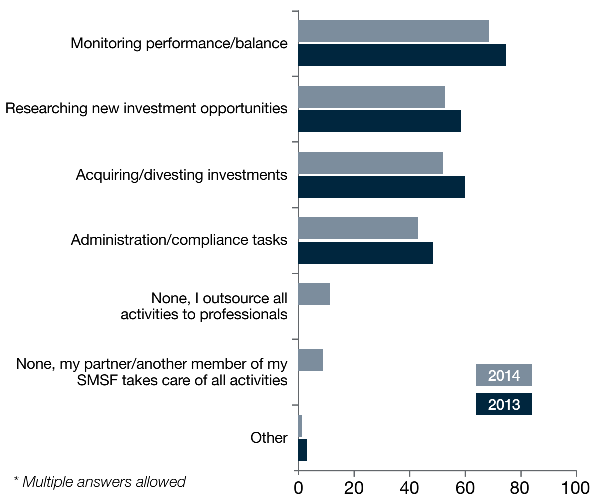
Tasks in which trustees are becoming less personally involved include monitoring their SMSF's performance/balance, researching new investment opportunities and acquiring/divesting investments. The majority (56.6%) of trustees are not personally involved in administration/compliance tasks, up from 51.2% in 2013.

The new breed of trustee is looking for support and guidance in managing their fund and represents the biggest growth opportunity for advisers, accounting for the majority of the sector (Figure 2).

Close to half (45.9%) of trustees are classified as coach seekers, compared to 43.9% in 2013, while 15.0% are outsourcers, up from 11.9% in 2013. These behavioural profiles are more amenable to financial advice and view SMSFs not so much as a DIY option but rather a 'help me do it' solution to superannuation savings.

Another potential new opportunity for advisers is the growth in young people setting up an SMSF. In line with the ATO's statistics showing the increase in younger SMSF members, the Intimate with Self-managed Superannuation Report found that in the last two years, close to two thirds (65.7%) of advisers have experienced

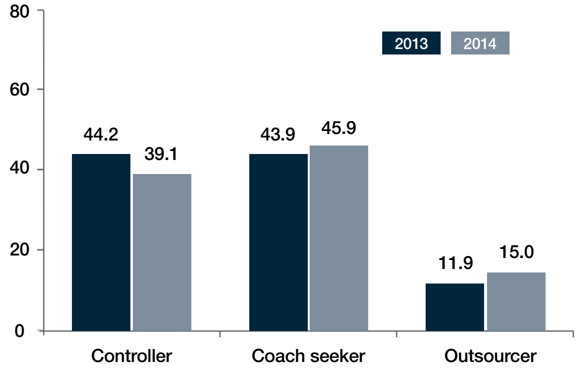
Figure 1. Which of the following activities are you personally involved in for your SMSF?



* Multiple answers allowed

Source: Intimate with Self-managed Superannuation Report 2015

Figure 2. Behavioural Segmentation



Source: Intimate with Self-managed Superannuation Report 2015 growing demand for SMSF advice from 31–40 year olds, while more than one in five (21.7%) have witnessed an increase in demand from 20–30 year olds. However, despite the fact that younger trustees are the most likely to find most SMSF-related tasks challenging, particularly keeping up with compliance, the report found the majority of trustees aged 40 and under do not currently receive financial advice. If advisers are to tap into this younger cohort of trustees, they will need to appeal to the preferences of this age group – who tend to be digitally-savvy and information hungry. CoreData's Digital Intimacy Report[4] revealed more than half (58.5%) of respondents aged 29 and under spent at least 11 hours online for leisure purposes each week, with a fifth of those (22.4%) spending more than 20 hours. Almost a third (31.4%) spent at least 11 hours a week on social media. To appeal to this market, advisers must have an online presence, in particular a website that clearly articulates their value proposition to this demographic, and be active on social media outlets such as Twitter, Facebook and LinkedIn.

The key advice needs of the younger demographic differ to Baby Boomer and Pre-boomer generations and include saving, tax, insurance and family financial matters. CoreData's Australia Advised Study[5] of Australians in a relationship with a financial adviser found those under 40 were more likely to perceive that the greatest advantages of using an adviser were feedback and opinions on investment choices, help with financial planning and goal setting, and general information on how to invest, while those over 40 were more likely to cite advantages such as access to investment and superannuation expertise and help maintaining discipline related to financial investments. These differences suggest young people with an adviser see them as more of a sounding board – someone who they can test their own ideas with and who can help them get the right structures in place to allow them to take control of their financial future. They view the adviser not so much as an expert to whom they can outsource decision-making, but as a partner who can assist them in achieving their goals, and place high value on convenience.

4 CoreData Digital Intimacy Report, September 2015
5 CoreData Australia Advised Study, September 2015

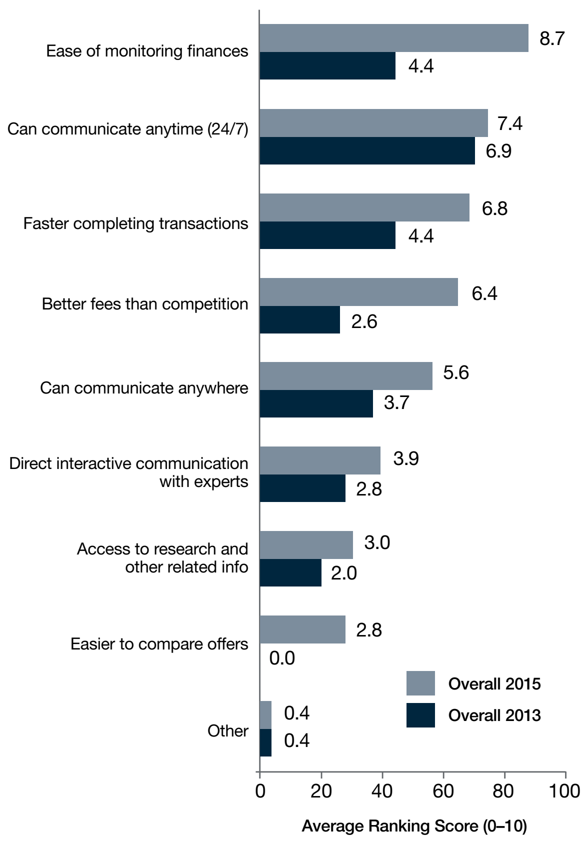
Adviser opportunities

Advisers looking to tap into the younger trustee market will need to make sure their customer value proposition highlights the services that are high on this cohort's priority list. Given their desire for convenience and the breadth of support younger trustees are likely to require over their lifetime, advisers that offer a 'one-stop-shop', leveraging the latest technology, are best placed to access this new market. Specialists still have a key role to play in providing SMSF advice to clients, particularly to controllers, however the Intimate with Self-managed Superannuation Report found high demand for a full service proposition among the broader trustee market as well, suggesting we could see broader advisory models in the future. More than half of trustees (50.4%) who derive their investment and asset allocation strategies with support from an adviser prefer a one-stop-shop offer that covers all of their needs. In response to the demand, advisers are increasingly offering in-house SMSF services, with more than three in five (63.7%) advisers offering tax advice in 2014, up from 45.9% in 2013, and more than half (50.7%) providing compliance services, up from 36.6% in 2013.

Millennials tend to be more digitally driven, and while their investable assets might be lower than their older counterparts, their readiness and enthusiasm for using technology makes them prime candidates for engagement via digital technology platforms. The so-called 'race to zero' has seen increasing downward pressure on financial services fees due to greater competition, shifting consumer expectations and unbundling of value driven by legislative reform targeted at increasing transparency and technological innovation. These developments mean that transactions, administration and implementation are expected to be delivered at a lower cost. Platforms that provide a fully integrated system for advisers, accountants and their SMSF clients to partner on the establishment and management of SMSFs are likely to gain traction among the younger trustee market due to their functionality, convenience and transparency. However, advisers must find a way to bring forward the future benefit of financial advice for young trustees. Present value may be generated via responsiveness to triggered needs, engaging content and communications, digital tools and delivering peace of mind in the present. The Digital Intimacy Report reveals that in the last two years, convenience and competitive fees have become increasingly important but are now just 'tickets to play' – advisers must satisfy these two key elements if they have any hope of winning new business from young trustees (Figure 3).

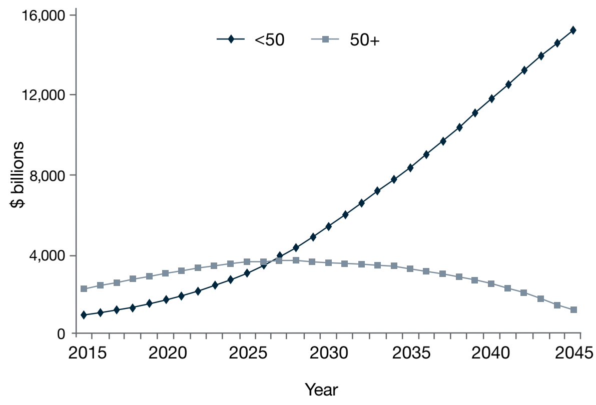
A decade from now, the rise of the alphabet generations truly kicks in and there will be a 'passing the funds under management' torch moment, when the value of investable assets held by the under 50s surpasses the value of investable assets held by the over 50s. Advisers that have done the ground work and already adapted their business models to appeal to this new segment will find that their business is in a good position to capture the intergenerational wealth transfer that will occur over the next 30 to 40 years (Figure 4).

Figure 3. When choosing a channel to communicate with your financial services provider, what are the most important benefits to you?



Source: CoreData Digital Intimacy Report, 2015

Figure 4. Projected value of investable assets



Source: CoreData

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