The Australian Super - Hostplus
Active vs Passive Experiment

Australian Super and Hostplus have, for the last 7 years – to June 2019 - offered both actively managed and indexed options to investors. These options have the same levels of expected risk (5 negative years in 20 in each case) and broadly the same return objectives (CPI + 4%, and CPI + 3% for the actively managed and indexed options respectively).

The options offered by each super fund are based on the same investment expectations, are constructed by the same investment teams, managed using the same information, and have the same administrative structures. These can truly be said to be 'experiments', in that all extraneous factors have been 'controlled for' with the exception of directly attributable to investment fee differences.

As would be expected, the actively managed Balanced (normal cost) options have higher investment costs than the indexed Balanced (low cost) options. (54 basis points lower for Australian Super and 69 basis points for Hostplus.)

Returns to June 2019

The option returns for period to June 2019 are set out in the following tables:

Table 1: Australian Super Active vs Indexed

Option	1 Year	2 Years p.a.	3 Years p.a.	5 Years p.a.	7 Years p.a.
Balanced (Active)	8.67%	9.87%	10.72%	9.48%	10.96%
Indexed Diversified	8.74%	9.07%	8.94%	7.48%	8.83%
Active Outperformance	**-0.07%**	**0.80%**	**1.78%**	**2.00%**	**2.13%**

Table 2: Hostplus Super Active vs Indexed

Option	1 Year	2 Years p.a.	3 Years p.a.	5 Years p.a.	7 Years p.a.
Balanced (Active)	6.80%	9.21%	10.80%	9.65%	11.13%
Indexed Balanced	8.51%	9.06%	9.46%	8.23%	10.54%
Active Outperformance	**-1.71%**	**0.15%**	**1.34%**	**1.42%**	**0.59%**

Unsurprisingly, given the performance of some equity strategies, the active options did relatively less well over the past year.

It is notable however that over all periods of 2 years or longer, the active options have materially and consistently outperformed their indexed equivalents.

These results are presented in graphical format in Charts 1 & 2.

Chart 1: Australian Super Active vs Indexed

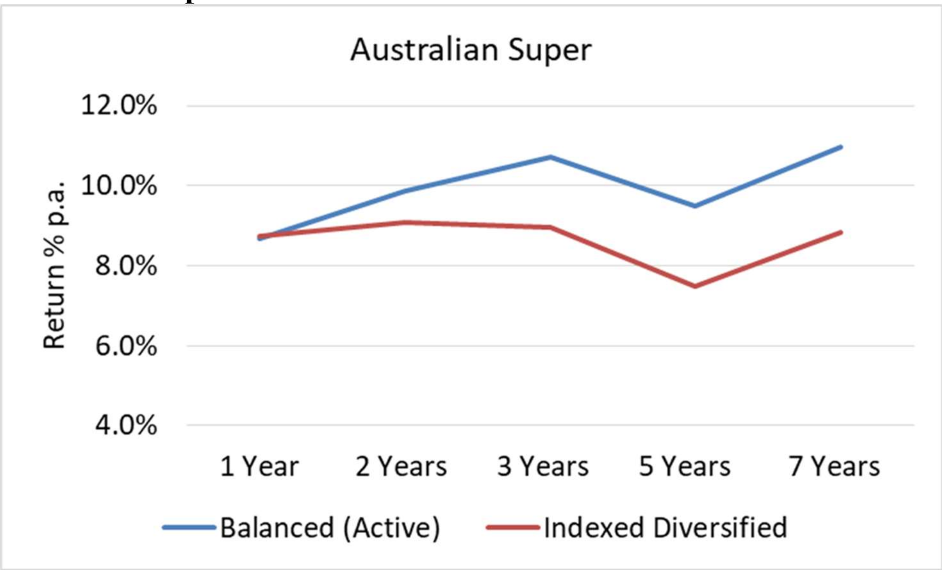
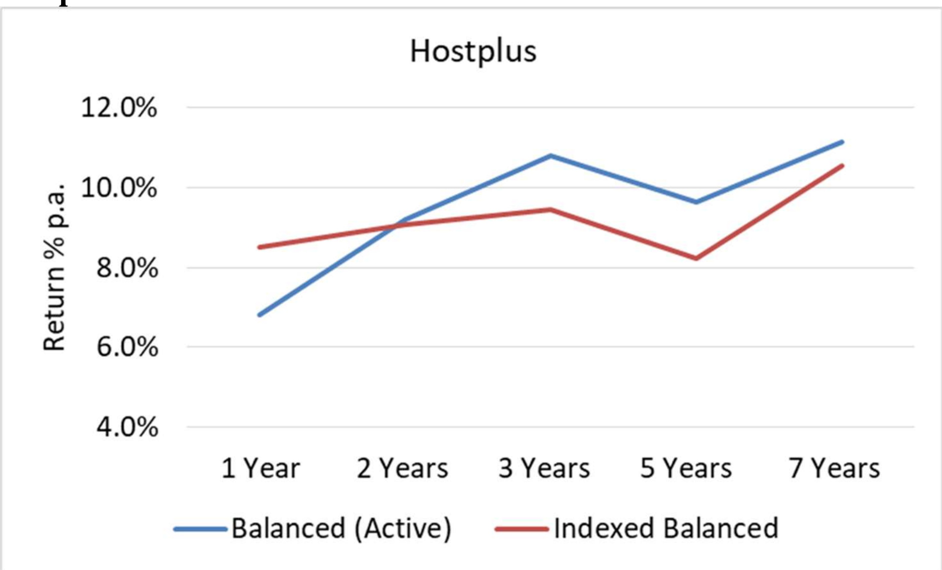


Chart 2: Hostplus Active vs Indexed



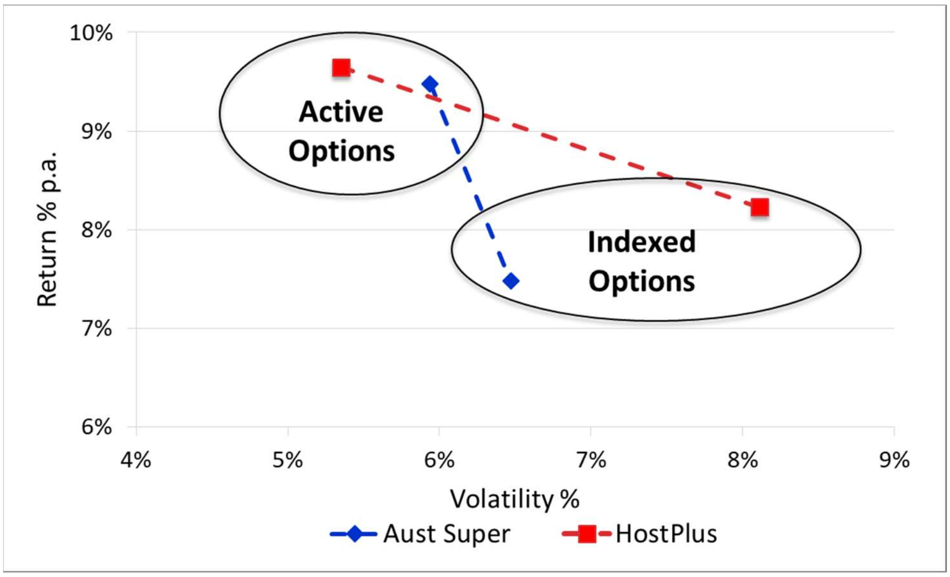
These are real investment options with actual superannuation fund members' retirement savings invested in them. The active 'normal cost' options have materially and consistently outperformed their indexed 'low cost' equivalents over relevant time frames.

Volatility of Returns

Volatility is a proxy – albeit a poor one – for the level of portfolio risk that investors experience. In general, less risk is preferred to more risk for the same level of investment returns.

As noted above, Australian Super's and Hostplus's actively managed options have materially outperformed their indexed options in terms of returns. They have also done so with lower levels of volatility!

Chart 3: Volatility / Return Comparisons



Why does this result occur?

It is a common mistake to confuse 'Low Cost investment' with 'Indexed investment', however this only reflects a small part of the picture.

On one hand, 'Indexed investment' implies the use of low cost investment strategies in some asset classes – typically equity and fixed interest – by minimising the use of manager skill.

On the other hand, 'Low Cost investment' implies both the use of indexing in some asset classes, as well as the avoidance of those asset classes that only exist in conjunction with manager skill – such as direct credit, infrastructure, hedge funds, private equity and direct property.

Thus, a 'Low Cost' investment strategy means investing only in market risks, and not having access to the wide range of return generation and diversifying non-market investment risks available. Thus a 'Low Cost' investment strategy will have lower investment risks – and hence lower returns – while being less diversified, and therefore have greater portfolio risk.

This is the outcome that we have seen in the past, and can expect to continue to see in the future, from the Australian Super – Hostplus, active vs indexed experiment.

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