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SUBMISSION

Submission to ASIC – Australia's evolving capital markets: *Discussion Paper*

28 April 2025

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Executive Director, Markets

Australian Securities and Investments Commission

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Via email: markets.consultation@asic.gov.au

28 April 2025

Dear Sir/Madam

Australia's evolving capital markets

The Association of Superannuation Funds of Australia (ASFA) is pleased to provide this submission in response to the Australian Securities and Investments Commission's discussion paper on the dynamics between public and private markets.

About ASFA

ASFA, the voice of super, has been operating since 1962 and is the peak policy, research and advocacy body for Australia's superannuation industry. ASFA represents the APRA regulated superannuation industry with over 100 organisations as members from corporate, industry, retail and public sector funds, and service providers. We develop policy positions through collaboration with our diverse membership base and use our deep technical expertise and research capabilities to assist in advancing outcomes for Australians.

We unite the superannuation community, supporting our members with research, advocacy, education and collaboration to help Australians enjoy a dignified retirement. We promote effective practice and advocate for efficiency, sustainability and trust in our world-class retirement income system.

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If you have any queries or comments in relation to the content of our submission, please contact [redacted] ([redacted]@superannuation.asn.au), or [redacted] ([redacted]@superannuation.asn.au).

Yours sincerely

[redacted]

Chief Policy and Advocacy Officer

Introduction

Summary of ASFA's position

Superannuation funds maintain rigorous governance and oversight, ensuring professional standards in private market investments. While retail investors may seek greater control, any increased focus by ASIC for retail investment should prioritise governance and transparency to protect outcomes. Coordination between ASIC and APRA is essential to avoid duplicated efforts, increased compliance costs, and risks to member returns. Strong public markets remain critical for private market exits like IPOs, while for private markets careful consideration of disclosure is needed to safeguard intellectual property and private market competitiveness.

Key points:

- **Institutional expertise in private markets**: Superannuation funds and asset consultants conduct rigorous due diligence, ongoing monitoring, and engagement. As ASIC examines private markets, it is important that it considers the professionalism, governance, and sophistication of the institutional investment framework, which ensures member protections.
- **Continuous improvement within a strong governance framework**: While the industry remains open to enhancements, ASFA believes that current governance and protection measures in the institutional space are robust.
- **Balancing retail access with investor protections**: Retail investors can already access private markets through superannuation funds, but greater individual control should be accompanied by strong governance, transparency, and disclosure to safeguard sustainable outcomes.
- **Regulatory efficiency and member outcomes**: Collaboration with APRA has strengthened valuation and fee transparency (e.g. RG97). Additional regulatory measures should carefully consider their net impact, as increased compliance costs could reduce member returns.
- **Avoiding regulatory overlap**: With APRA already applying heightened scrutiny, further regulation by ASIC may risk duplication, adding complexity and diverting resources from delivering strong returns for members. Effective coordination between regulators will support efficient oversight.
- **Thoughtful approach to transparency:** ASIC should carefully consider the balance between transparency and confidentiality, ensuring any additional disclosure supports regulatory oversight without unintended consequences. Disclosure directed to APRA rather than the public would help safeguard intellectual property and mitigate risks related to non-disclosure agreements. It is also important that transparency measures do not inadvertently affect competitive dynamics or the integrity of private market investments.
- **Competitiveness of Australian institutional investors**: Increased regulatory scrutiny could make Australia's private markets less attractive relative to other jurisdictions, potentially limiting global investment opportunities.
- **Interplay between public and private markets**: Strong public markets support private market exits, such as IPOs and trade sales, affecting superannuation fund allocations between domestic and offshore equities.
- **Managing concentration risks in public markets**: Rising passive investing by superannuation funds may increase market concentration, a dynamic that differs from the diversification benefits of private markets.

Background to private markets and the superannuation industry

The growing size of the superannuation system

For the APRA-regulated superannuation system, the total value of investments currently stands at $2.7 trillion (end of December 2024). The value of superannuation investments has more than doubled over the past decade (from $1.2 trillion in December 2014), with an average annual growth rate over that period of 8.2 per cent.

At the system level, new financial capital in the order of $40 billion needs to be deployed to new investments each quarter, on average. Actual quarter-to-quarter investment requirements can vary markedly. This reflects the volatility of key components of system-wide inflows and outflows – particularly voluntary contributions and investment income for re-investment.

Superannuation funds' broad approach to asset allocation

With respect to superannuation fund investments, the over-arching legal requirement on the trustee of a fund is to make investments that are in the best financial interests of the beneficiaries (members) of the fund. To this end, superannuation funds are required to set investment objectives in respect of each investment option, and to formulate a corresponding investment strategy to achieve those objectives.

At the asset-class level, fundamental to determining the appropriate allocation is the risk-return trade off – that is, for a given risk tolerance, the asset-class mix that has the best chance of achieving investment objectives. There are numerous, sometimes competing factors that determine ultimate asset allocation at the strategic level, and within asset classes, and thus the ultimate allocations to public and private assets. A non-exhaustive list is below.

- Diversification: superannuation funds diversify their investments across and within asset classes to reduce exposure to risks associated with; countries, industries, technologies, individual entities (and more).
- Liquidity management: asset allocation needs to accommodate liquidity/cash-flow requirements, and ensure that the fund's liquidity needs can be met at all times. This includes the impact of market downturns on member requests for switching between investment options and for redemptions.
- Membership profile: investment preferences can differ across age cohorts. For example, compared with fund members in the accumulation phase, retired members can have a greater preference for 'defensive' assets such as fixed-income securities compared with 'growth' assets such as equities.
- ESG considerations: a fund's investment objectives can incorporate ESG considerations, where these are consistent with the outcomes the fund seeks to provide members. Related asset-allocation strategies – including ESG exclusions, filters and tilts – are guided by these considerations.

Investment strategy can be thought of as agnostic as to whether a particular asset is public or private, but instead influenced by the particular features of an asset and its potential for delivering on investment objectives for members.

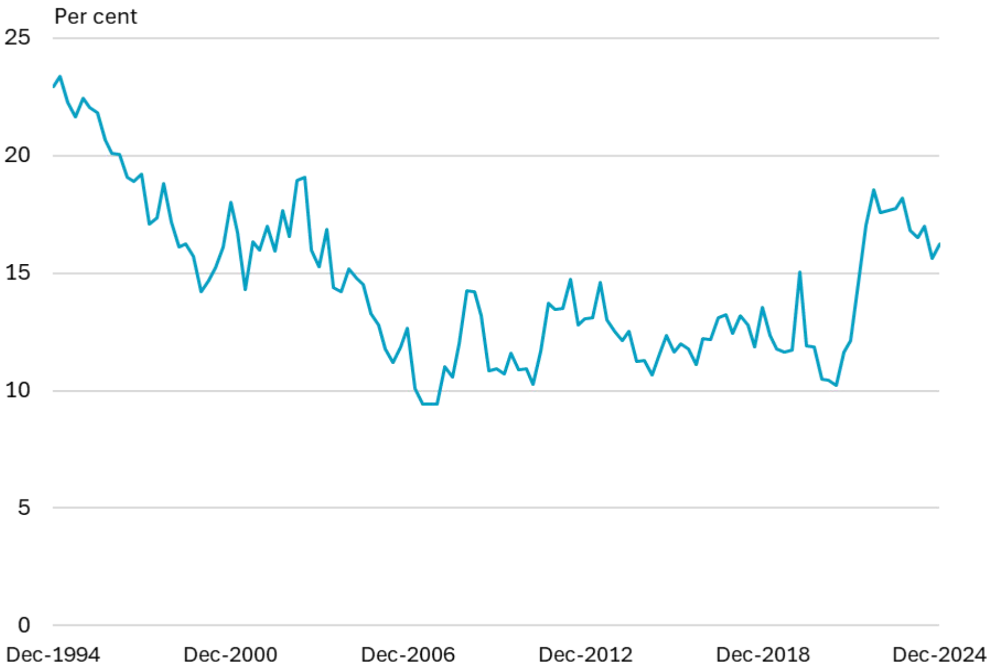
The size of private markets in Australia

For Australia, data on the overall size of unlisted markets is limited. The most complete data relates to unlisted equity – which is published by the Australian Bureau of Statistics.

For total equity (listed and unlisted) issued by Australia's corporate sector (financial and non-financial corporate entities), and held by Australian institutional investors (superannuation funds, insurance companies, other investment funds), Chart 1 shows the proportion that is unlisted equity.

Over the past three decades the proportion for unlisted equity has averaged around 15 per cent, where short-term movements largely reflect valuation changes for listed equities. The unlisted proportion rose sharply during the early part of this decade – which reflects the sharp fall in the listed equity market during the early stages of the COVID-19 crisis, coupled with net purchases of unlisted equity assets. That said, the current proportion remains within its longer-term range.

Chart 1: Domestic corporate unlisted equity held by Australian institutional investors
Proportion of total domestic corporate equity held by Australian institutional investors



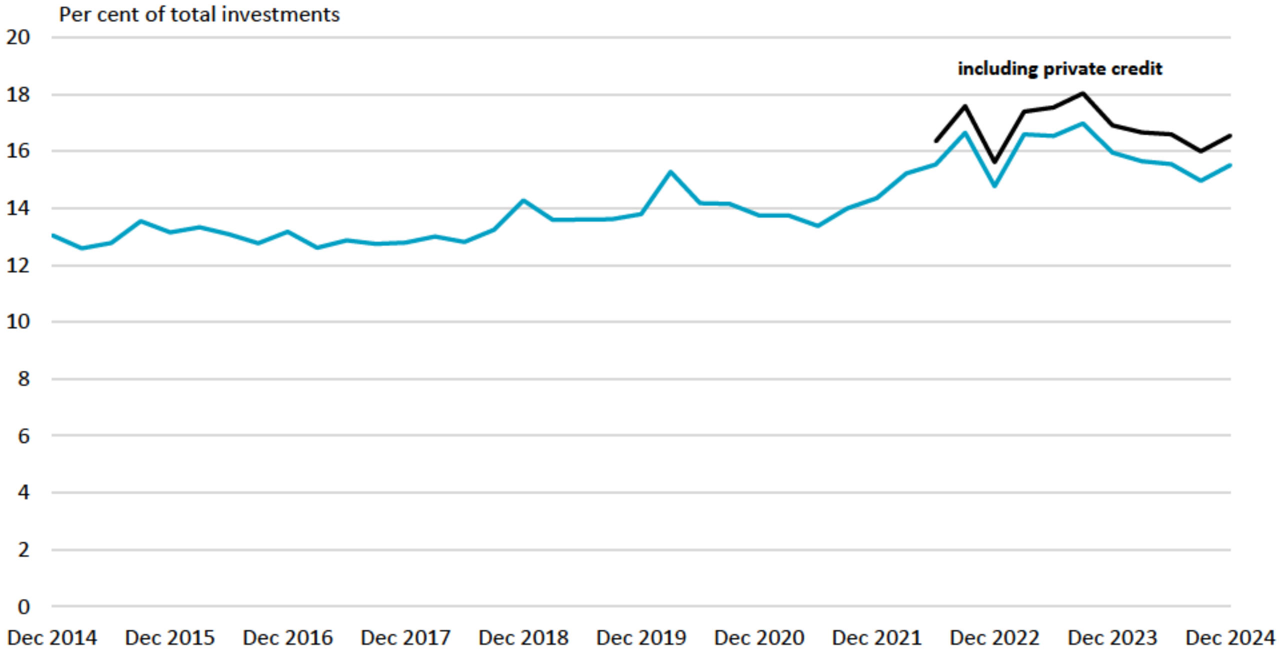
Source: ABS and ASFA calculations.

Superannuation funds have a long history of private-market participation

As a collective, APRA-regulated superannuation funds have been long-time participants in private markets – both in Australia and offshore. This is evidenced by the fact that the proportion of total superannuation investments that is allocated to private/unlisted assets has risen only slightly over the past decade.

Excluding private credit (for which the available time-series data starts at June 2022), the proportion for private/unlisted assets increased from 13.1 per cent in December 2014 to 15.5 per cent in December 2024, or by 2.4 percentage points over the 10-year period (Chart 2). With respect to the current proportion (December 2024) that incudes private credit, private/unlisted assets comprise 16.6 per cent of total superannuation investments.

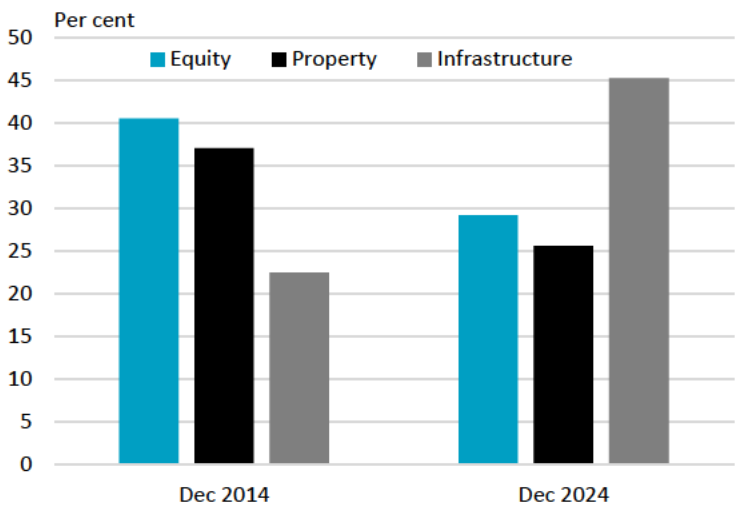
Chart 2: Superannuation investments in private/unlisted assets
Proportion of total superannuation investments



Source: APRA and ASFA calculations.

More consequential changes have occurred to the composition of fund investments in private assets. For total private/unlisted assets investments, Chart 3 shows the proportions for each of the three key asset classes (again, excluding private credit due to lack of data). In particular, over the past decade, the proportion for infrastructure has increased from under one-quarter of total private assets to almost one-half. For the period where data on fund investments in private credit is available, the proportion for private credit (within total fund investments in private assets), has increased from 5 to 6 per cent.

Chart 3: Superannuation investments in private/unlisted assets
Proportions by asset class



Source: APRA and ASFA calculations.

This shift in asset allocation reflects numerous factors, including the changing relative attractiveness of asset classes (and of particular assets) within the context of diversified investment portfolios, as well as the flow of new investable assets in Australia and overseas. With respect to the rising share for infrastructure, it also reflects a greater degree of familiarity with, and expertise in unlisted infrastructure as an investable asset class within the broader superannuation ecosystem.

Looking forward: funds' allocation to private assets

The potential trajectory for allocations to private market asset classes will be influenced by several key factors.

For real estate, economic conditions, urbanisation trends, and sector-specific demand (for example, healthcare, life sciences, data centres and logistics) play crucial roles. Infrastructure investments are driven by government policies, the need for sustainable energy, and the defensive nature of these assets. Private equity allocations are influenced by market conditions, regulatory environments, and the potential for high returns (particularly in growth and buyout strategies), with the *Your Future, Your Super* framework adding an additional layer of complexity given the listed-market nature of the performance benchmark. Venture capital investments depend on technological advancements, innovation trends, and the ability to commercialise new technologies. Lastly, affordable housing investments are shaped by government incentives, regulatory frameworks, and the balance between perceived risks and returns.

The potential trajectory for asset allocations is also dependent on a range of general factors, notably current valuations, views on the forward-looking macroeconomic environment (for example, GDP, inflation and cash rates), and competitive market dynamics (for example, continued fee pressure). These factors collectively determine how superannuation funds allocate their resources across different asset classes.

Anecdotally, funds plan to continue to allocate to these sectors.

Benefits of private assets

Risk/return profile of private asset classes

Superannuation funds invest in private assets as part of a wholistic portfolio approach designed to deliver the best possible risk-adjusted returns to members. In this regard, private assets can provide particular benefits to diversified investment portfolios, which compliment investments in public assets.

Private assets offer significant diversification benefits, encompassing a broad range of asset classes such as unlisted infrastructure, unlisted property, private equity, and private debt or credit. Each of these asset classes has distinct risk and return profiles, spanning the growth spectrum—from high-growth opportunities like private equity to mid-risk investments such as property and infrastructure, and low-risk options like private credit, depending on portfolio credit ratings.

These varying characteristics not only enhance diversification but also contribute to portfolio resilience by enabling superannuation funds to strategically balance risk and return. Compared to public assets, private assets often exhibit low or even negative correlations with other investments, which supports more stable, long-term returns for members. Furthermore, factors such as current valuations, macroeconomic conditions, and competitive market dynamics (for example, fee pressure) play a crucial role in shaping asset allocation strategies, and ensure that private market investments align with broader portfolio goals.[1]

[1] Frontier (2022), *Super in the Economy: The Investment Opportunity in Australian Private Markets*.

In addition to diversification, private or unlisted assets represent a compelling avenue for elevated investment returns. A key advantage lies in their ability to generate an illiquidity premium – an additional return that compensates investors for holding assets that are not readily convertible to cash. This is particularly evident in real, unlisted assets such as infrastructure and commercial property. Superannuation funds, with their long-term investment horizons, are well-positioned to capitalise on the illiquidity premium where it exists – thereby potentially enhancing long-term returns for members.

Unlisted property investments are particularly appealing for their ability to deliver stable and predictable returns, with lower volatility compared to public markets. As a reliable option for long-term growth, unlisted property provides steady income streams, while offering the potential for capital appreciation – making it an attractive asset class for superannuation portfolios.

Infrastructure assets, such as essential services like toll roads and renewable energy projects, are highly valued for their defensive characteristics and consistent cash flows. These assets typically provide lower risk and steady returns due to their critical role in the economy and long-term contracts that ensure stable income. For example, toll roads benefit from predictable traffic volumes and regulated toll rates, while renewable energy projects, such as wind and solar farms, often have long-term power-purchase agreements that guarantee revenue. Additionally, infrastructure investments are less sensitive to economic cycles, making them a reliable choice for risk-averse investors seeking stability and resilience in their portfolios.

Private equity, although higher on the risk spectrum, offers the potential for substantial gains, particularly through growth and buyout strategies that unlock value in emerging businesses or underperforming assets. These investments are often characterised by their ability to drive transformative change within companies, making them a high-reward option within a diversified portfolio. Venture capital, as a subset of private equity, provides significant upside potential by supporting innovations in technology and other pioneering sectors. While inherently high-risk, it offers the promise of exceptional returns through the commercialisation of groundbreaking technologies and disruptive business models.

Affordable housing investments, bolstered by increased government support and incentives, deliver both social impact and potential financial benefits. Additionally, private debt and credit offer relatively predictable income streams, with varying risk levels depending on credit quality.

Together, these diverse characteristics position private market assets as powerful contributors to long-term, risk-adjusted returns in superannuation portfolios.

Potential over-regulation of private assets risks perverse outcomes for members. It could lead to reduced long-term returns to members or impact the economic case for some of the above asset classes.

The real economy

Ultimately, the (new) private assets to which superannuation fund allocate financial capital are a source of funding for the Australian business sector. The funding raised by business entities through a variety of debt and equity offerings – including via private markets – is used by those entities to fund new fixed capital investment and innovation, and to provide working capital and to smooth cash flows.

From a broader macroeconomic perspective, the financial system's ability to allocate funding efficiently to the real economy – that is, to activities with the highest potential economic returns – is central to promoting higher trend rates of economic growth for the Australian economy, and higher levels of living standards for the Australian population.

For business entities, a broad range of different potential funding mechanisms supports higher allocative efficiency.

For any business entity, decisions around the preferred form of financing, at a particular point in time, reflects a range of factors – including the maturity of business entity, the particular purpose of any tranche of financing, the relative cost and availability of different forms of financing, and the entity's current (and expected) mix of debt and equity. For any business entity, changes in this regard will be reflected in the preferred form of financing – including preference for private sources of financing such as private equity or private debt.

Undue barriers, regulatory or otherwise, risks limiting and/or raising the cost of financing for business. More broadly, reducing allocative efficiency in the economy implies lower levels of gross fixed capital investment than otherwise would be the case, and lower levels of long-term GDP.

Australia's economic transformation

For the Australian economy, the superannuation system is an increasingly important source of capital – both debt and equity – for new investment that underpins Australia's long-term productivity performance, our energy transition and social objectives. Looking ahead, a regulatory environment that supports fund allocations to private/unlisted assets will facilitate real investment in the Australian economy.

New infrastructure investment is a key source of productivity growth in modern economies. Particularly in the context of the recent rapid increase in Australia's population, Australia has a significant infrastructure needs. The available international comparisons suggest that, notwithstanding recent increases in government spending on infrastructure and increased private participation in projects, the overall quality of Australia's infrastructure lags behind some comparable nations.[2]

Australia's journey to achieving net zero emissions will require a fundamental transformation of Australia's capital stock – such that the emissions generated from the production of all goods and services in the economy (in a given period) nets to zero, and all within a timeframe of little more than a single generation. For Australia, as is the case globally, this structural shift will require higher, sustained levels of new fixed capital investment in the real economy than otherwise would be the case. Future fixed capital investment will be concentrated among a set of key sectors – most notably the energy sector.

Superannuation funds have been increasingly involved in funding affordable housing by utilising various investment approaches. These include: build-to-rent and build-to-rent-to-own models, where funds invest in housing developments for rental purposes with a potential pathway to ownership for renters; and debt financing, where funds provide loans to community housing providers. Funds also form partnerships with governments and other stakeholders to pool resources and facilitate larger-scale investments in this sector. These investments aim to generate appropriate risk-adjusted returns for members, while addressing social needs.

Stricter regulatory requirements concerning private assets, particularly private debt, could impact the risk/return trade-off for such investments, and reduce investor appetite. Regulatory requirements could include those aimed to address regulator concerns about valuation complexities, liquidity risks, and the lack of transparency in private debt markets.

Significantly amending regulation for private assets would likely impact investment appetite for structures with Government involvement, such as affordable housing. Increased regulatory scrutiny may also lead to heightened compliance and reporting requirements, affecting operational costs and investment processes.

[2] World Economic Forum, *The Global Competitiveness Report 2019: Insights Report* and the International Institute for Management Development's World Competitiveness Rankings.

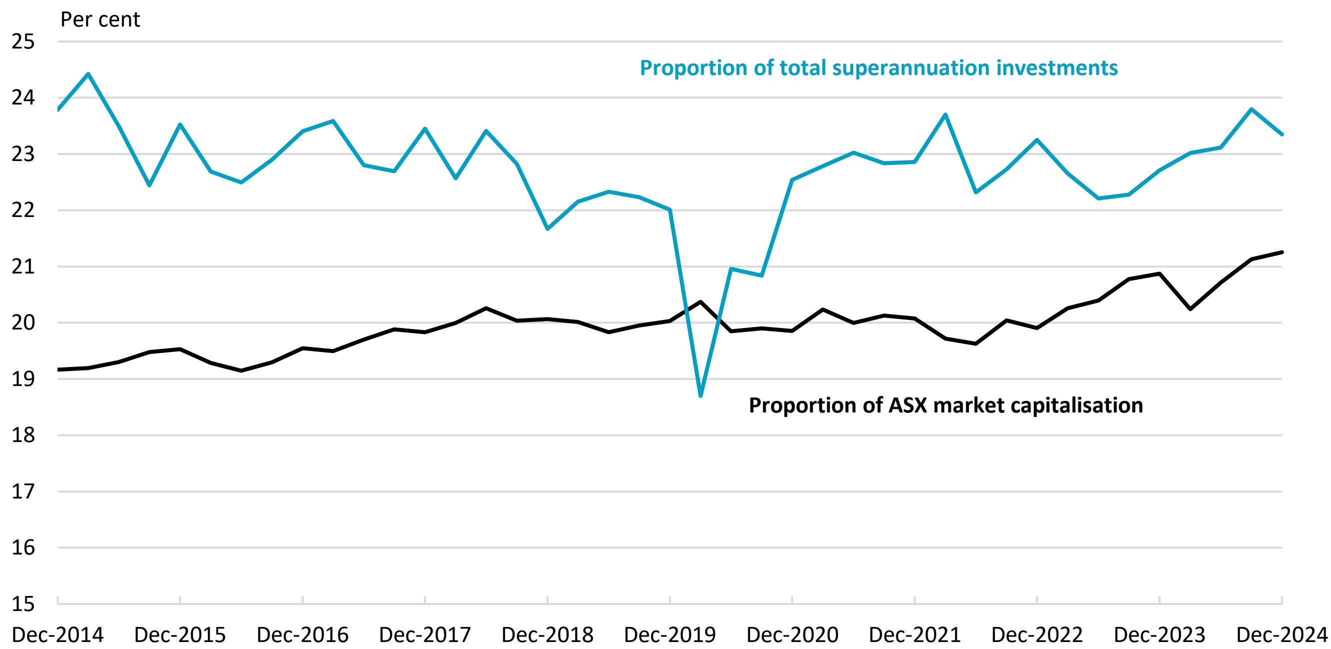
Interaction between public and private markets

Superannuation fund investments in domestic listed equities

The counterpoint to superannuation funds' investments in private markets is their investments in public markets. As noted above, the proportion of total superannuation fund investments that is allocated to private assets has increased only slightly over the past decade. The majority of superannuation investments are allocated to public assets. Domestic public assets currently account for almost 40 per cent of total superannuation investments.

Australian superannuation funds continue to have a strong appetite for Australian listed equities. As a proportion of total superannuation investments, Australian equities have maintained a fairly constant share over the past decade: from 23.8 per cent in December 2014 to 23.3 in December 2024, with an average of 22.7 per cent during this period (Chart 4), noting that the volatility in the proportion held over this period largely reflects general market movements in the ASX (relative to other asset classes).

Chart 4: Superannuation fund investments in listed Australian equities



Source: ABS, APRA and ASFA calculations.

Indeed, over the past decade, superannuation fund holdings of Australian listed equities have represented a rising share of the total market capitalisation of the ASX – from 19.2 per cent in December 2014 to 21.3 per cent in December 2024. That said, for the superannuation system as whole, there is likely an upper bound to this share. This largely reflects the concentration risk associated with greater exposure to the domestic equity market.[3]

[3] In aggregate, superannuation funds exhibit a home-country bias with regards to domestic listed equities. At the system-level, the ratio of domestic listed equities to international listed equities is around 40:60. On the other hand, the market capitalisation of the ASX accounts for just 2 per cent of global equity market capitalisation.

Public markets: the regulatory framework

Australian financial market licensees have a statutory obligation (under section 792A(a) of the *Corporations Act 2001*), to do all things necessary, to the extent that it is reasonably practicable to do so, to ensure that each of its licensed markets is fair, orderly and transparent.

ASIC has primary responsibility for administering financial market regulation. Among its main regulatory functions (as set out in *ASIC Regulatory Guide 172 Financial markets: Domestic and overseas operators*), is responsibility for assessing and enforcing operators' compliance with their obligations.

- ASIC also has frontline responsibility for supervising secondary trading activity taking place on licensed financial markets, as well as making and ensuring compliance with the ASIC market integrity rules.

Market licensees are required to have operating rules that apply to the market they are authorised to operate. Operating rules (including listing rules) deal with activities or conduct of the market, and activities or conduct of persons in relation to the market.[4]

Rules for the listing of entities (*Corporations Regulations 2001 – Reg 7.2.07*), include those that relate to:

- admitting an entity to the official list of the licensed market for the purpose of enabling financial products of the entity to be traded on the licensed market, and removing an entity from the official list; and
- activities or conduct of an entity that is included on the official list of the licensed market, including a description of the arrangements for the disciplining of the entity for a breach of the operating rules.

Listing rules for public markets

Public companies in Australia are required to promptly disclose material information to ensure transparency and keep investors informed. They must provide annual financial reports, including audited accounts, and follow principles-based recommendations for governance, such as board composition, risk management, and shareholder rights. Significant transactions, like mergers or acquisitions, must be disclosed and may require shareholder approval if mandated by the ASX. Companies must also meet minimum shareholder spread requirements, adhere to rules for restricted securities, and can request trading halts to manage market-sensitive information.

Caution in applying public listing rules to private companies

We caution ASIC around any consideration of applying public listing rules or governance standards to private companies. While adopting certain public company listing rules could enhance transparency and accountability for private companies, it is important to acknowledge the differences between the two sectors. Public company regulations are designed for entities with broad shareholder bases and market exposure, whereas private companies operate within distinct frameworks and structures. Applying similar rigour to private companies may impose unnecessary burdens without proportional benefits. Therefore, caution should be taken to avoid imposing undue complexity that may not yield significant advantages.

[4] *ASIC Regulatory Guide 172 Financial markets: Domestic and overseas operators*.

Superannuation funds operate under a robust regulatory framework

Regulatory framework for investing by APRA-regulated superannuation funds

APRA-regulated superannuation funds are subject to a robust, comprehensive regime for investment governance – in particular, APRA's *Prudential Standard SPS 530 – Investment Governance* (SPS 530), but also complementary standards that cover issues such as; broader fund governance (*Prudential Standard SPS 510 – Governance*) and outsourcing of fund operations (*Prudential Standard SPS 231 – Outsourcing*).

From APRA's perspective, the ultimate purpose of its investment governance regime is to ensure that superannuation funds (RSE licensees) prudently select, manage and monitor investments on behalf of fund members – consistent with their fiduciary obligations to act in the best financial interests of members.

In broad terms, APRA's investment governance regime relates to the adequacy of systems, structures, policies, processes and people. In this regard, under APRA's Prudential Standard *SPS 530 Investment Governance*, RSE licensees must have in place:

- periodic reviews of investment objectives and investment strategies
- due diligence processes for the selection of investments
- measures to monitor the performance of investments on an ongoing basis
- comprehensive investment stress testing
- a liquidity management plan
- an effective valuation governance framework.

In general, APRA expects that where a licensee chooses to undertake investment functions in-house, the licensee's systems, policies and resources are to be comparable with those of an external, highly-skilled service provider that undertakes an equivalent activity. Use of external providers must be accompanied by the appropriate degree, and frequency of oversight by the licensee.[5]

APRA periodically reviews its investment governance regime to ensure it remains fit for purpose and also assesses governance practices across the superannuation industry. APRA's most recent update to SPS 530 focused on enhancing requirements for valuations and liquidity management.

APRA's most recent review of investment governance arrangements noted improvements (since the prior review) to investment decision-making and governance practices across the industry, but also identified areas for improvement.[6] In its thematic review of valuation practices, APRA noted a variation in approaches across the industry. The most common issues that APRA identified for improvement relate to management of conflicts of interest arising from investment staff being involved in the valuation process, and demonstrated challenge to external valuations (see next section).[7]

The superannuation industry acknowledges the importance of robust valuation governance, particularly in light of increasing allocations to private markets. Funds are actively enhancing their practices in several key areas, including the establishment of independent valuation committees and the use of external specialist advisors – both of which serve to reduce potential conflicts of interest where investment teams are responsible for valuations. Further, there is a general increase in Board or Committee involvement in

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[5] APRA, *Prudential Practice Guide SPG 530 – Investment Governance* (updated January 2023).
[6] APRA, *Strengthening Investment Governance – Consultation*, Letter to RSE Licensees, 29 September 2021.
[7] APRA, *Governance of Unlisted Asset Valuation and Liquidity Risk Management in Superannuation*, December 2024.

valuation processes, providing additional oversight. Many funds are also implementing public market triggers that prompt a review by independent teams to determine whether a valuation update is required.

Superannuation funds undertake rigorous due diligence and monitoring of investments

In this section, we delve into the governance practices and rigorous due diligence processes that superannuation funds employ when reviewing and monitoring new investments.

For any emerging asset class, familiarity and expertise within the institutional superannuation ecosystem builds over time. For any fund, decision-making with respect to investment in any asset is guided by their investment governance framework – which is applied generally. In this regard, the quality of investment governance is critical – including sound processes for the selection, management and monitoring of investments on behalf of fund members that are agnostic to the form of investment.

Superannuation funds and their asset consultants engage in a rigorous investment and operational due diligence process when investing in private markets. This includes background checks and performance analysis of fund managers, detailed evaluations of investment strategies, and comprehensive reviews of operational infrastructure and compliance frameworks.

Financial health and valuation methods are scrutinised to ensure transparency and consistency. Legal documentation and regulatory compliance are reviewed, and on-site visits and interviews with key personnel are conducted to gain deeper insights. This extensive due diligence ensures that investments align with strategic objectives and risk tolerance, providing a level of scrutiny and oversight far beyond what is typically available to retail investors.

Monitoring and valuations are also critical components of superannuation funds' investment strategies in private markets. Superannuation funds benefit from a high degree of transparency in mandates and pooled trusts, allowing them to closely monitor the performance and risks associated with their investments. A growing number of superannuation funds also have sizeable internal investment teams, which allows for more focused monitoring of existing assets or manager investments.

Additionally, valuation processes relating to private market investments have been reviewed and strengthened recently following extensive industry consultation and interaction with APRA. This contrasts with retail investors, who may not have the same level of insight or access to timely valuation updates, making it more challenging to assess the true value of their investments.

APRA oversees comprehensive regulatory data collection

APRA collects detailed data from superannuation funds through its reporting standards, covering critical areas such as asset allocation, liquidity, investment exposures, and net returns. This framework already provides comprehensive insights into fund operations and risks.

The existing standards ensure regulatory supervision is well-supported without imposing extra burdens on funds. For this reason, it is important that ASIC consider this burden if seeking additional data requirements. We would suggest that APRA should gather any extra data to ensure data submission is efficient for funds.

Concerns around additional regulation and potential unintended consequences

Example: annual superannuation performance test

The benefits of any potential regulatory change should be assessed against any likely costs or unintended consequences. The operation of the annual superannuation performance test provides a recent example of the unintended consequences of regulation on investment behaviour and the implications for member outcomes.

The annual superannuation performance test, while not mis-aligned with member outcomes, does influence funds' investment behaviour such that asset allocation and approaches to risk management differ from what otherwise would have been the case (in the absence of the performance test).

In particular, in order to manage portfolios against the current performance metric, funds invest with regard to their budget for tracking-error vis-à-vis the prescribed test benchmarks. While products with a relatively large performance buffer (vis-à-vis the portfolio benchmark) can tolerate a larger tracking error budget in the short-term, all products are subject to a (sustainable) long-term tracking error budget. This can act as a constraint on asset allocation decisions.

The effects (of needing to manage tracking error) on asset allocation decisions are likely to be more consequential for assets/asset classes that are not well-represented by the existing set of benchmarks – where allocations to affected asset classes would be lower than otherwise (in the absence of the performance test). This includes the broad range of unlisted assets, but particularly unlisted 'greenfield' investments in private equity and infrastructure.

Potential duplication of regulatory effort

Given the increased regulatory scrutiny already being applied by APRA, any additional regulatory burden imposed by ASIC in this area could lead to a duplication of efforts. This could divert resources from superannuation funds' core focus of maximising returns for members and potentially create unnecessary complexity and compliance costs. It is crucial that regulators coordinate effectively to ensure a streamlined and efficient regulatory environment for private market investment.

Comparison of Australia's regulatory regime with other jurisdictions

Regulatory approaches to private market assets vary across jurisdictions. Australia emphasises prudential oversight (APRA) and market integrity (ASIC), while the US focuses on disclosure (SEC). The UK and Europe prioritise transparency and investor protection, with a growing emphasis on sustainable finance. Canada uses a mix of provincial and federal oversight, focusing on risk management. This reflects different market structures and regulatory philosophies.

Australia's robust regulatory settings, relative to other jurisdictions, provide a strong framework for investor confidence. However, increased regulatory scrutiny, including potential ASIC actions, may create an environment that could inadvertently affect the competitiveness of Australian institutional investors in global private markets. If fund managers perceive Australia as less favourable, it may lead to higher fees to attract them or limit access to top-tier managers, which could ultimately impact member return outcomes.

Transparency and disclosure

Transparency/disclosure of unlisted assets

ASFA considers that the current regulatory regime supports an adequate degree of transparency and disclosure with respect to fund investments in unlisted assets. ASFA acknowledges that some increased disclosure could be helpful, although is concerned about the public nature of any increased disclosure.

Public disclosure could risk exposing commercially-sensitive information, potentially undermining competitive strategies and intellectual property protections. It is crucial that any additional measures strike a balance that enhances transparency while safeguarding member interests and preserving the integrity of private market operations.

Superannuation funds have a high degree of internal transparency

In effect, members of a superannuation fund delegate investment-related decisions to their fund – which is under a legal obligation to make investment decisions that are in the best financial interests of its members. This arrangement is fundamental to trust law, under which superannuation funds operate.

For a member's superannuation fund, APRA's investment governance regime supports transparency around unlisted investments required for informed investment-related decisions by the fund and by external providers of investment services (to the fund), on behalf of fund members. External service providers include investment managers, but also asset consultants, which provide a broad range of investment-related functions, such as:

- for investment options, designing strategic asset allocation to meet performance objectives
- recommending investment strategies and managers for specific asset classes
- monitoring performance of investment options and investment managers.[8]

This 'internal' transparency is fundamental to making informed investment-related decisions that are in the best financial interests of fund members. However, there are risks associated with disclosure of more detailed investment-related information to fund members.

ASIC should consider the challenges of broader public disclosure of investment-related information. Such disclosure could pose risks, including commercial sensitivity, potential market disruptions, and the likelihood of misinterpretation. It may also conflict with legal obligations, such as non-disclosure agreements, or create administrative complexities for funds. Maintaining a balanced approach to transparency can ensure that institutional processes remain effective while safeguarding the interests of fund members.

Impacts of greater member transparency

Higher costs

For individual fund members, ASFA considers that the current disclosure regime strikes an appropriate balance between the benefits and costs to members. This includes the combined impact, on consumer-facing disclosure, of the current regimes for Product Disclosure Statements and Portfolio Holdings Disclosure.

Greater, more granular disclosure would increase both direct and indirect opportunity costs for individual fund members.

Direct costs of greater, more granular disclosure is the cost of additional disclosure requirements on funds, where higher costs ultimately would be passed on to members as either lower investment returns or lower quality/quantity of services. The direct cost impact of additional disclosure requirements largely would relate to the additional cost of compiling the information. To the extent that any new disclosure regime would overlap with, or duplicate other existing disclosure regimes, direct cost impacts also would relate to the cost of complying with that new regime.

There is also likely to be indirect opportunity costs to members. Broadly speaking, opportunity costs would relate to forgone investment returns: for example, where a highly-regarded global fund manager decides to

[8] Under a typical trust deed, superannuation fund trustees have wide powers of delegation with respect to their functions, and typically outsource many of their functions to entities that are external to the fund. It is important to note that although funds outsource many of their functions, they cannot outsource their responsibility for the performance of those functions – a fundamental tenet of trust law.

not bring its product to Australia to avoid any perceived excessive regulatory disclosure/transparency burden.

Balancing transparency and competitiveness in private markets

For a superannuation fund, the decision to invest in particular private/unlisted assets reflects the accumulation of knowledge and expertise – within the fund and/or external investment service provider – with regard to the particular assets and the broader asset classes. The investments represent the intellectual property of the fund and/or external investment service provider (in particular, asset consultants and investment managers).

There is a trade-off between perfect transparency and the ability for Australia to be a functioning, attractive destination for private market investments. Increased public disclosure requirements for fund managers pose significant risks, particularly concerning the protection of intellectual property. Mandatory disclosure of portfolio holdings can expose proprietary investment strategies, leading to potential replication by competitors and loss of competitive edge. This transparency, while beneficial for investor confidence, may deter global fund managers from operating in markets with stringent disclosure norms, such as Australia. Additionally, other market participants/competitors could exploit the disclosed information to their advantage, ultimately harming a strategy's performance – which ultimately would impact the superannuation fund and its members.

If greater, more granular disclosure would require funds to disclose such information publicly, then this information also would be available to competitor funds and external investment service providers. It also could be contrary to non-disclosure agreements that typically are in place between institutional investors and the recipients of institutional financial capital (see next section). A key risk is that greater, more granular disclosure would have a harmful effect on new investment by superannuation funds in affected asset classes.

Moreover, local disclosure can inadvertently telegraph private details about global portfolios. Australian investors might be investing into a local vehicle that serves as a feeder fund into a global investment vehicle. This means that disclosing the holdings of the local vehicle could reveal sensitive information about the broader global strategy, compromising the confidentiality of the global fund's positions and strategies. This interconnectedness underscores the need for a balanced approach to disclosure that protects both investor interests and the strategic integrity of fund managers.

At the system level, reduced investment appetite among superannuation funds for a particular asset class(es) would likely lead to a lower level of allocated financial capital to that asset class(es) by superannuation funds. Over the long term, this could reduce the financial viability of particular projects in the real economy – such as commercial property and infrastructure projects – with flow-on effects to broader economic activity and employment.

Members of superannuation also would be affected. As noted above, unlisted/private assets provide benefits to diversified investment portfolios, which compliment investments in public assets, reflected in higher long-term investment returns for members. To the extent that funds, over the long term, would have a lower allocation to particular asset classes(es) than otherwise would be the case, long-term investment returns for members also would be lower.

Contrary to non-disclosure agreements

Increased disclosure requirements can conflict with existing non-disclosure agreements (NDAs) between funds and their managers, as well as between managers and the underlying investments or loans within their portfolios. These NDAs are designed to protect sensitive information, ensuring that proprietary strategies, investment details, and confidential business practices remain secure.

By mandating extensive public disclosure, these agreements could be breached, exposing sensitive data that was intended to remain private. This would not only undermine the trust and legal commitments established through NDAs but would also risk revealing competitive strategies and confidential terms of underlying investments or loans. Such breaches could lead to legal disputes, loss of competitive advantage, and potential financial harm to both the fund managers and their clients.

Therefore, while transparency is important, it must be carefully balanced with the need to honour confidentiality agreements and protect sensitive information.

Considerations for retail investors

Retail investors can already access private markets through superannuation funds. However, greater individual control should be accompanied by strong governance, transparency, and disclosure to ensure sustainable outcomes. In this section, we differentiate between retail investors, who seek direct investments into products offered by fund managers, and superannuation funds, which have a fiduciary duty to invest in private market products on behalf of their members (the end retail investors). The key difference between these approaches is direct control versus fiduciary activities performed by superannuation fund trustees on behalf of the members.

Anecdotal evidence suggests that retail interest in private/unlisted assets appears to be rising, and with it a rising allocation of savings of retail investors. ASFA considers that an uplift to disclosure requirements for retail investors would be desirable.

As is the case for any asset class, key differences between retail investors and APRA-regulated superannuation relate to depth of expertise and resources available to select, manage and monitor investments, and the degree of transparency of investments.

For APRA-regulated superannuation funds, investment decisions in relation to private/unlisted assets are made within a framework that adheres to robust, high regulatory requirements that encompass the processes by which decisions are made, and the people who make decisions. The same robust, high regulatory requirements require ongoing performance monitoring of investments. As noted above, APRA-regulated superannuation funds have been long-time participants in private markets – both in Australia and offshore. ASFA considers that while the superannuation sector will always consider ways to improve governance and oversight of its private unlisted assets, ASFA’s view is that the current regulatory settings strike the right balance – providing adequate internal transparency required for informed investment-related decisions made on behalf of members.

In contrast, for retail investors, private, unlisted assets represent an emerging asset class, where general knowledge of the features of the various types of unlisted investments, and the risks associated with particular private/unlisted assets, is likely to be limited. In terms of investment vehicles available to retail investors, lack of transparency is a typical feature of liquid structures that hold illiquid assets. Superannuation, as a conduit into illiquid assets, represents a safer alternative for potential retail investors.

There are broader concerns associated with a rising level of retail investment in private/unlisted assets. General unfamiliarity with private/unlisted assets – and in particular, a lack of understanding of the nature of risks associated with those assets – could be reflected in poor investment choices and outcomes. If widespread, this could cause reputational damage to affected unlisted asset classes among the general public – which includes members of superannuation funds. From the perspective of superannuation funds, a key concern is that this could feed back to members’ investment preferences for lower exposures to affected asset classes. Ultimately, this could lead to lower allocations to those asset class(es), which would affect long-term investment returns.