Systemic impacts of ‘big super’

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January 2025

Systemic impacts of 'big super'

An investigation of the systemic effects of a large superannuation system containing large funds

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Summary version

Systemic impacts of 'big super'

An investigation of the systemic effects of a large superannuation system containing large funds

January 2025

David Bell and Geoff Warren

This note summarises a comprehensive report on the systemic impacts of 'big super' that considers the potential implications of a large superannuation (super) industry containing some very large funds for the Australian economy, financial markets and/or population. We describe the report and draw out the key themes and findings. Please refer to the full report for details.

Report overview

Increasing attention is being directed at whether the activities of super funds may have 'systemic' effects, with particular focus on the potential for adverse impacts. Against this background, we contribute a comprehensive report that takes a systemic perspective and aims to identify and discuss all related issues. We set out to provide a balanced account by highlighting beneficial, detrimental and debatable aspects of big super. That is, the report is about much more than just systemic risk.

The word 'systemic' alludes to an overall system and is usually taken to imply a focus on interconnections between system components. We apply a different and wider lens. We define 'systemic' for the purpose of the report as: "*aspects of the super system that have widespread and significant implications for either the Australian economy, Australian financial markets or a significant number of Australians*".

Figure 1 (see over) frames up the interactions that are considered between three broad areas – the Australian economy, financial system and/or population; the superannuation sector (the collective of all funds); and individual super funds. Aspects that are denoted systemic need to have a significant impact on one or all of the three 'macro' components identified in the top box in Figure 1.

The width of the arrows that interconnect each area in Figure 1 represents our evaluation of the degree to which the interconnection is consequential. For instance, we consider impacts flowing from the broader macro environment to be quite consequential for the super sector and individual super funds. Meanwhile, the systemic impacts flowing up from the super sector are seen as moderately consequential and those flowing up from individual funds to be of limited consequence.

Key theme #1: Big super is a boon overall

Australia benefits from having a large super industry for four main reasons, which together well-outweigh any problems and risks:

- Super establishes a significant pool of retirement savings that may not have otherwise existed.
- Super funds operate as a vehicle for professional management of those savings by fiduciaries who are subject to various regulatory requirements.
- Super funds are well-positioned to act as effective stewards of the capital that they invest.
- The super sector rounds out the sources of finance within the Australian economy in ways not well-accommodated by other providers such as banks and direct investment by private investors.

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Thought Pieces with The Conexus Institute

Why severe liquidity stress in superannuation is hard to foresee

June 2025

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1. Introduction

In our *Systemic impacts of 'big super'* report of January 2025 (Section 5.3), we conclude that systemic liquidity stresses are *unlikely* to emerge from the super industry, albeit did not rule it out as a *possibility*. This thought piece summarises why we are relatively unconcerned about liquidity stress emerging from the super sector on a meaningful scale. In essence, our argument is that the confluence of events required for liquidity issues within super to escalate to a systemic level is ***quite unlikely***. There is a need to go through a series of 'stage-gates' before reaching a crisis state, the cumulative probability of which seems very low[1].

Nevertheless, we see greater risk that an *individual super fund* encounters significant liquidity stresses, which in turn causes significant harm to its members. The main reason is that it is more plausible that an individual fund could encounter some event that triggers widespread switching out of that fund (i.e. a 'run' on the fund). In contrast, at the system level it is far more likely that the assets will largely remain within the super industry. Further, losses borne by the members of a fund under pressure may amount to a gain for other players without any system-wide loss.

Liquidity management and potential for liquidity stress in superannuation (super) has recently been under focus by regulators. The Australian Prudential Regulation Authority (APRA) has given super funds a mixed report card on liquidity management practices; and is planning to conduct system-wide stress tests where liquidity issues are likely to play a central role. The Reserve Bank of Australia (RBA) notes in its *Financial Stability Review* of April 2025 that *"potential for financial system stress could be amplified if the superannuation sector faced severe liquidity stress … If several risks materialised simultaneously"* (see page 44), albeit suggesting that *"extreme but plausible conditions"*[2] were required for this to

[1] One of our stage-gates is that the authorities fail to take action to address any liquidity stresses amounting to a systemic threat, noting that the regulators are unlikely to flag the possibility of doing so. This may partly explain why we are more sanguine than the regulators, who are keen to avoid reaching this stage.

[2] The RBA states on page 40 of the Financial Stability Review that *"Structural features of the Australian superannuation sector help mitigate its direct threat to financial stability; however, in extreme but plausible conditions it could potentially pose an indirect threat by amplifying shocks in the financial system."*

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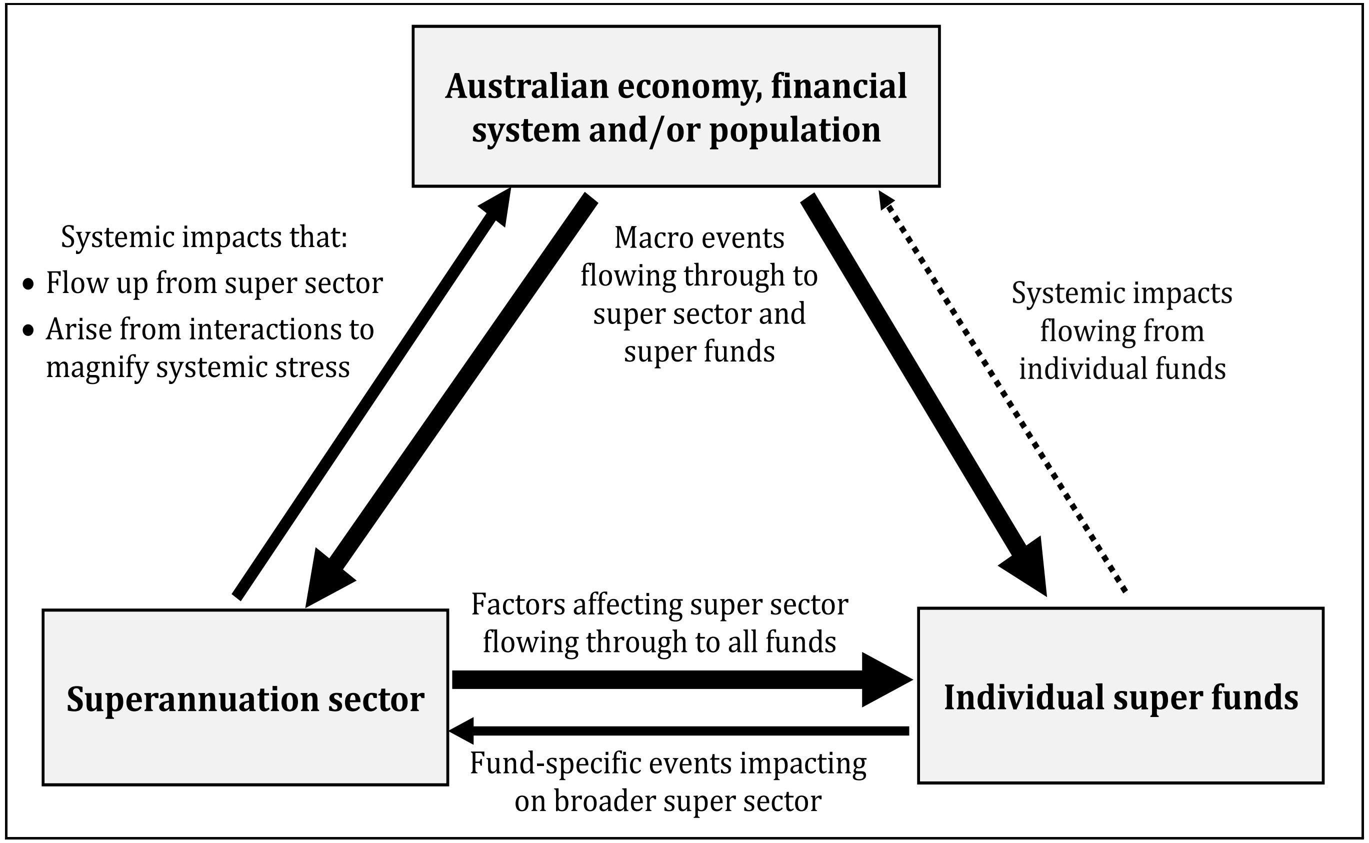
Systemic risks of 'big super' – Research approach

- We consider what impacts might arise from a big super system containing some very large funds for the Australian economy, markets and population at large
- We discuss beneficial impacts, risks and concerns, and issues to address
- System rather than individual fund perspective
- Extensive engagement around the draft



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Context: Australian super

- Predominantly defined contribution system with 12% contributions made by employers on behalf of all employees 18+ years of age

- Developing retirement / drawdown phase

- System is large and growing fast (circa 8% per annum growth)

Australian Dollars	Defined Contribution	Defined Benefit	Total Assets
APRA-regulated funds	$2.40t	$0.14t	$2.54t
Non-APRA-regulated public funds			$0.58t
Self-Managed Super Funds	$1.01t		$1.01t
			$4.13t

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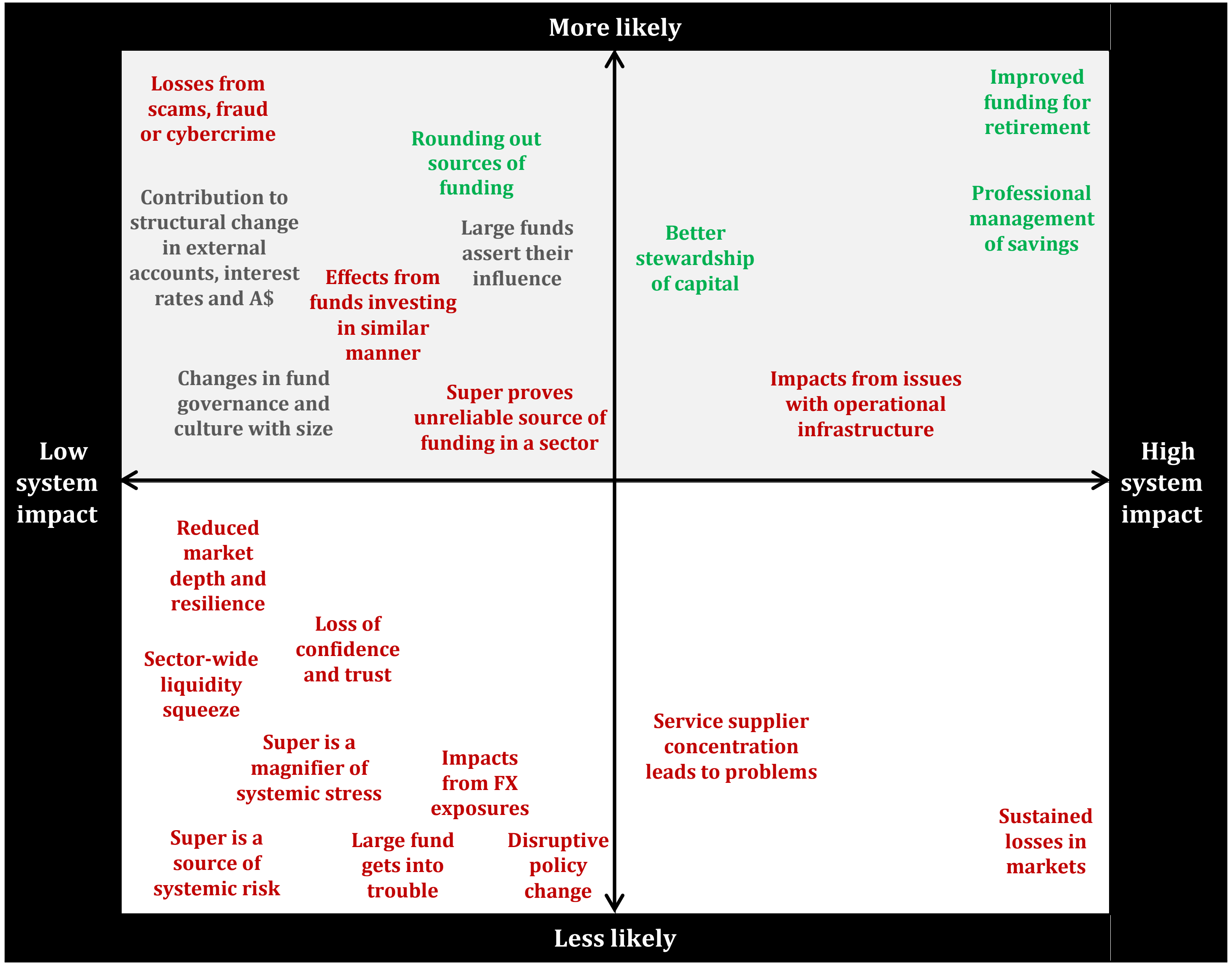
Systemic risks of 'big super' – Main takeaways

- Super is a boon overall
- While there are many issues to watch, two stand out:
  - Super heightens exposure to economic and market risk
  - Underdeveloped operating infrastructure within the super industry
- Super and systemic risk
  - Super is an unlikely source of systemic stress. Note: Risk of a liquidity event is overplayed
  - Whether super is a dampener or magnifier of system stress depends on the situation
- We are not ruling out individual funds getting into trouble and their members bearing the cost. But we don't view this as a systemic issue.

Systemic impacts – ‘weighed up’



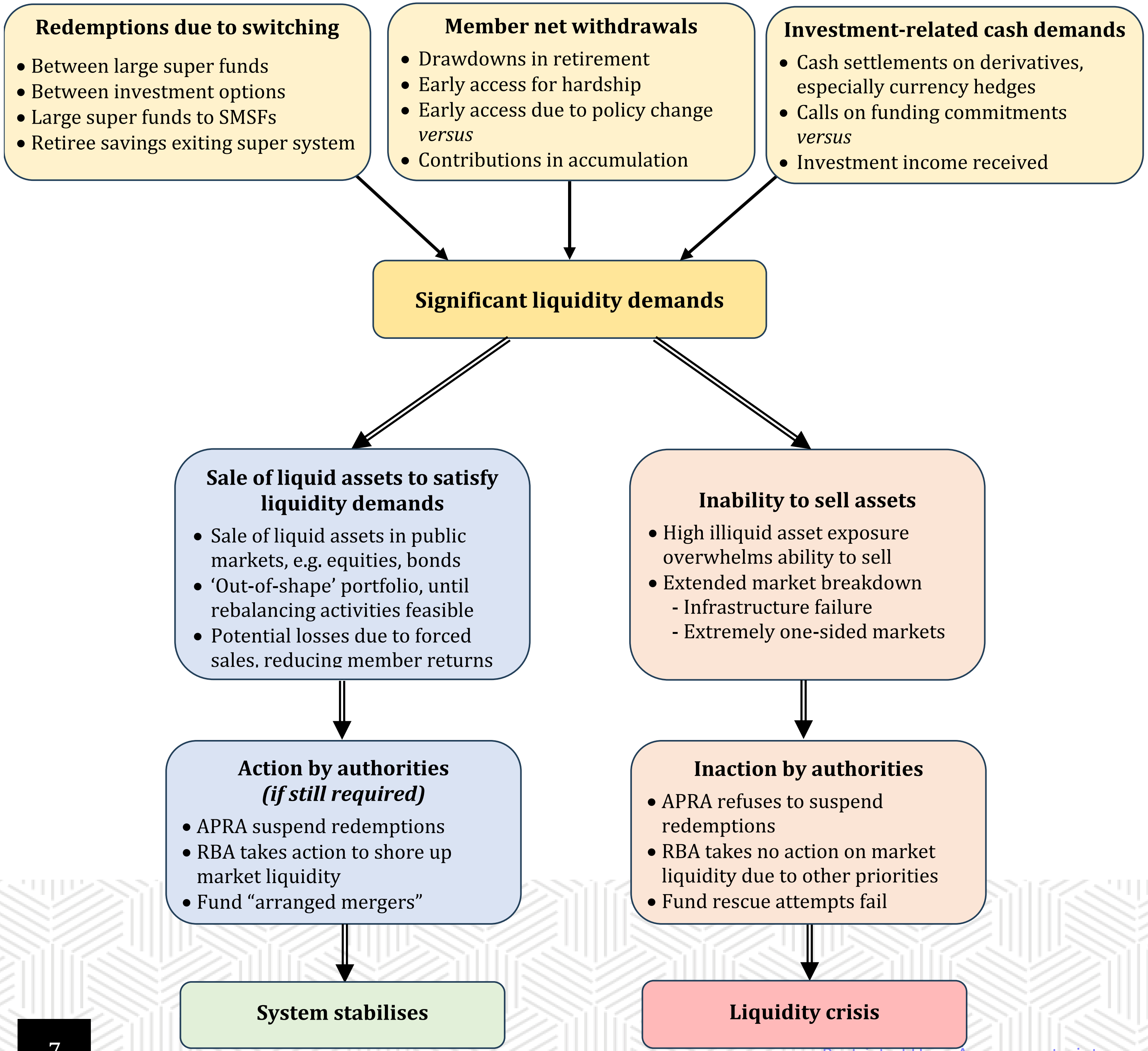
Legend:

Green *= beneficial effect*

Red *= potentially adverse effect*

Grey *= Mixed effect*

Stage-gates to a liquidity crisis



- Liquidity crisis requires going through the 'stage-gates' along the right branch
- Left branch is far more likely, resulting in the system stabilising
- We will be unpacking each level

Case 1 – Sensible starting position

Starting Position		
Illiquid assets 30%	Overseas assets (OA) 50%	Currency hedging of OA 50%

Market Movements and Flows Scenario
Modest
- Listed assets: -15%
- Unlisted assets: -10%
- AUD: -10%
- Net member flows: -5%

35% Illiquid Assets
Manageable

Market Movements and Flows Scenario
Difficult
- Listed assets: -35%
- Unlisted assets: -20%
- AUD: -20%
- Net member flows: -10%

42% Illiquid Assets
A little concerning

Case 2 – Stretched starting position

Starting Position		
Illiquid assets 40%	Overseas assets (OA) 50%	Currency hedging of OA 75%

Market Movements and Flows Scenario
Modest

- Listed assets: -15%
- Unlisted assets: -10%
- AUD: -10%
- Net member flows: -5%

47% Illiquid Assets
Problematic

Market Movements and Flows Scenario
Difficult

- Listed assets: -35%
- Unlisted assets: -20%
- AUD: -20%
- Net member flows: -10%

57% Illiquid Assets
Traumatic

Recommendations

For policymakers and regulators

Implementing policy change
- Consider systemic impacts
- Provide notice of policy changes, if at all possible

Areas where attention might be refocused
- Raise attention on system-level matters
- Consider systemic impact of YFYS performance test
- Take care not to undermine confidence in the super system

Potential points of vulnerability to investigate
- Operational infrastructure
- Scams
- Concentration in service providers

Matters where prior preparation seems required
- Possible run on a super fund or funds
- Overseas operations: monitoring, regulation, contingency planning

Issues to monitor
- FX hedging
- Use of influence by large funds

Other topics to research
- Impact of super on external linkages, specifically interest rates and A$
- Reliance of sectors on funding from super funds

For super funds

- **Invest and uplift practices** in two areas in particular:
  - Operational infrastructure
  - Risk management practices, notably liquidity stress testing
- **Industry collaboration** should occur in areas where issues are sector-wide, e.g. operational risk, cyber risk, scams, counterparty risk
- **Guard against loss of confidence and trust,** i.e. social license to operate

For media

While important to hold super funds to account, we call for responsible reporting that avoids unnecessarily undermining confidence and trust in the super system:

- Reporting should remain factual
- Avoid drifting into emotive and inflammatory language that entices fear
- Avoid leaving an impression the industry is universally failing when problems relate to individual funds; highlight both good and poor practice
- Communicate significance of any developments rather than focusing on numbers without context, e.g. scale relative to the super fund or sector

We welcome your questions and feedback

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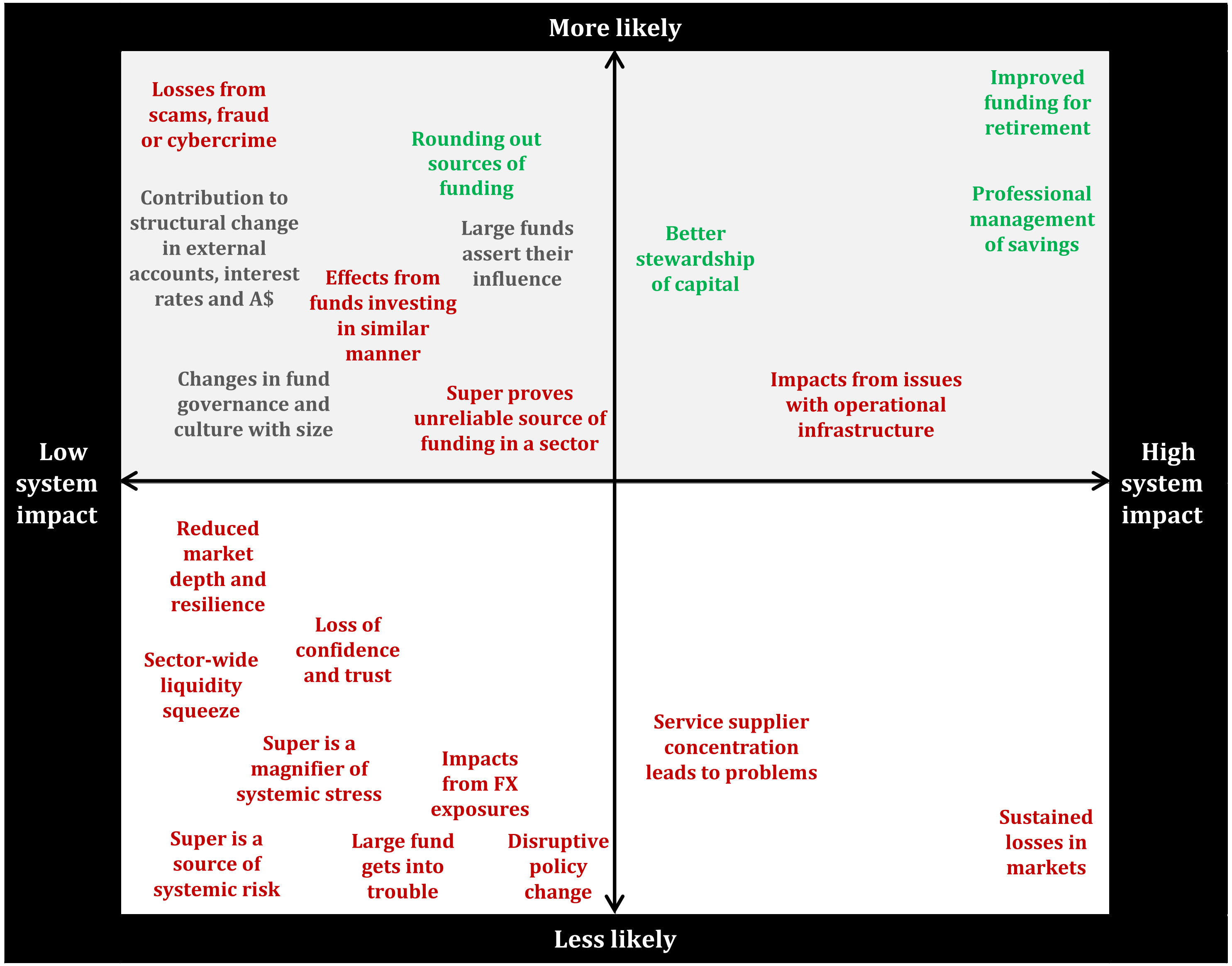
Appendix – Risk through three lenses

Systemic impacts – 'weighed up'



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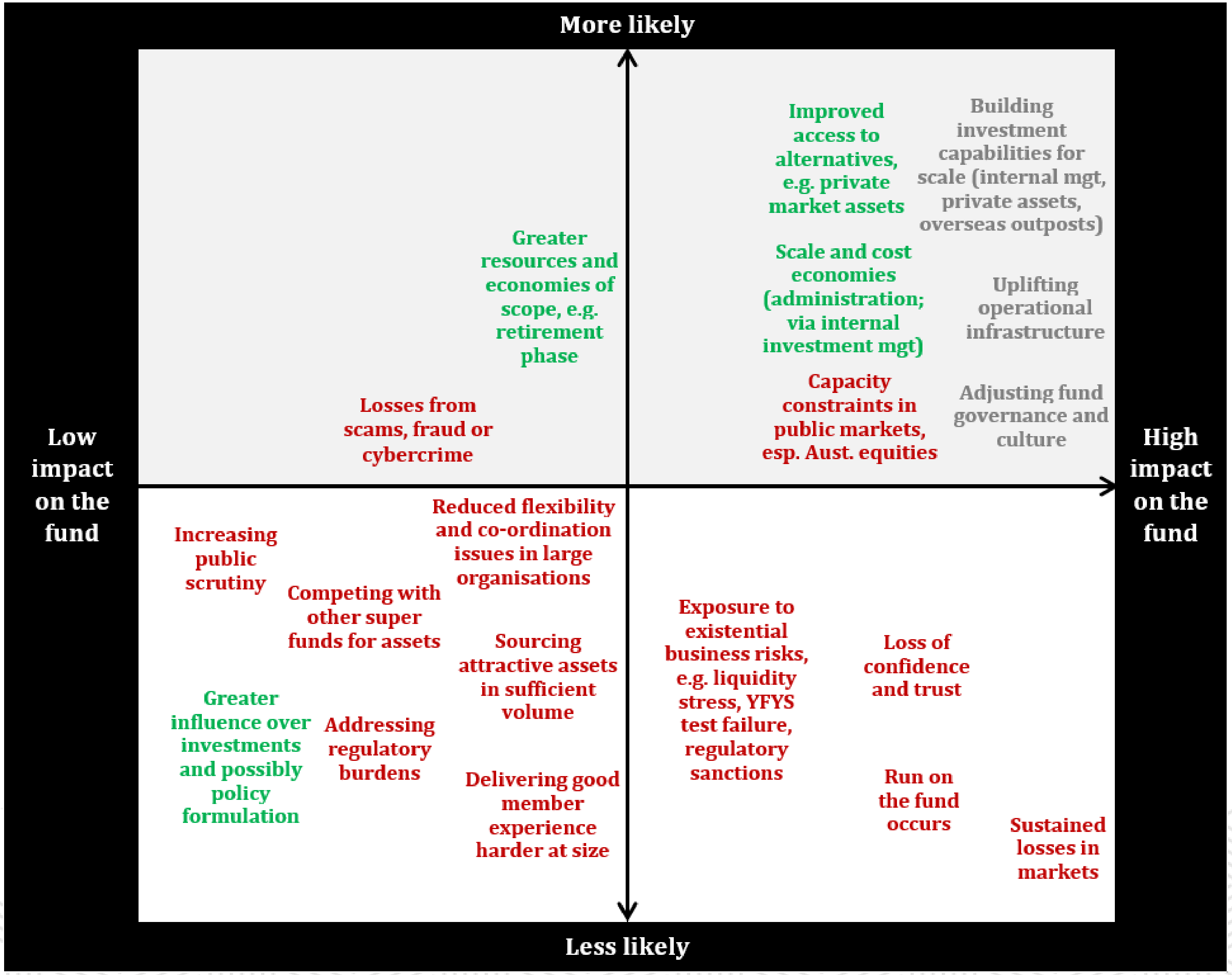
Super fund lens: Impacts from large fund size



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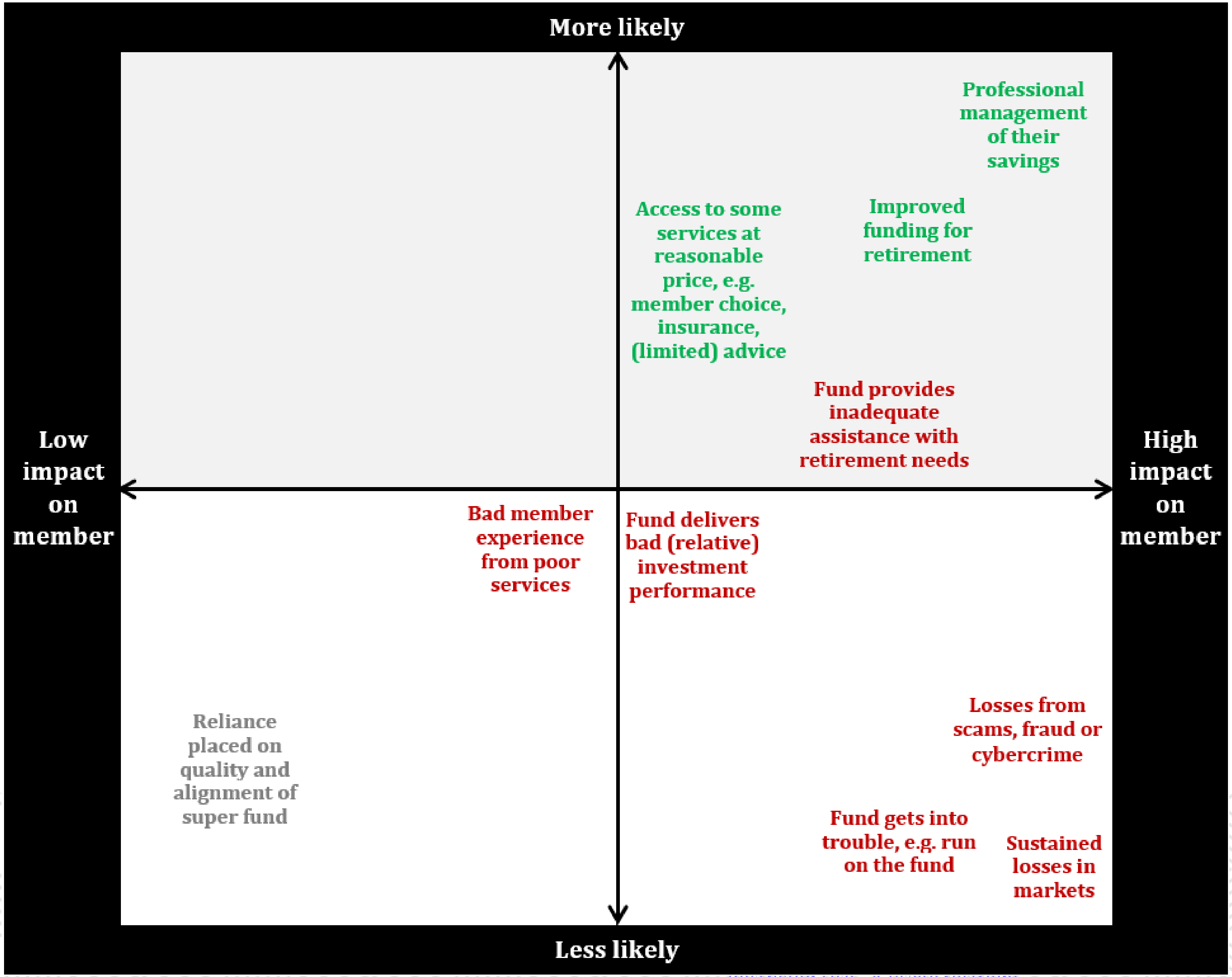
Member lens: Impacts from large investment in super



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