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Director
Members Outcomes and Governance Branch
Retirement, Advice and Investment Division
Treasury
Langton Cres
Parkes ACT 2600

By email: YFYS@treasury.gov.au

Superannuation Industry (Supervision) Amendment (Your Future, Your Super – Addressing Underperformance in Superannuation) Regulations 2023 (Draft Regulations)

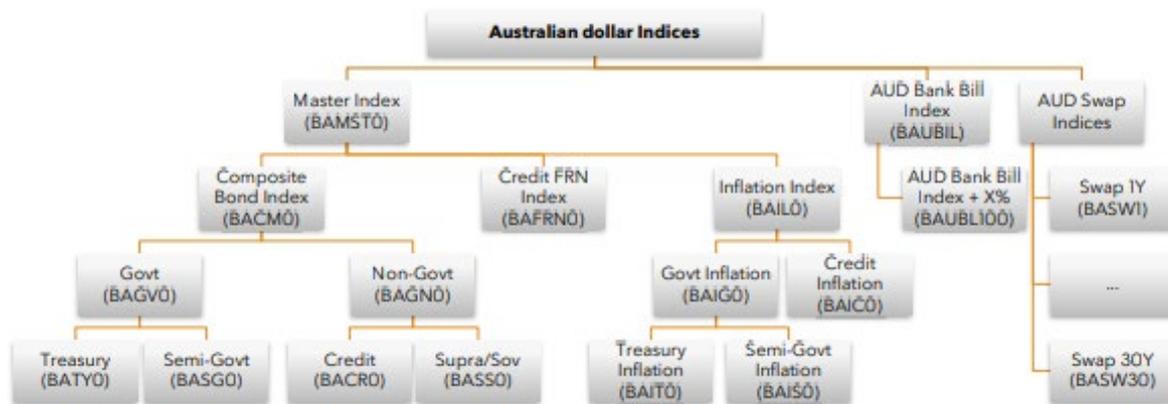
Introduction

The Australian Financial Markets Association (AFMA) welcomes the opportunity to provide comments on the exposure draft regulations, *Superannuation Industry (Supervision) Amendment (Your Future, Your Super – Addressing Underperformance in Superannuation) Regulations 2023 (Draft Regulations)*. AFMA represents the interests of over 120 market participants in Australia's wholesale banking and financial markets. AFMA's members account for more than ninety percent of all interbank, secondary market trading in debt and credit securities.

AFMA supports Treasury's decision to reference the alternative Master Index as the benchmark for fixed income products instead of the Composite index as this supports the inclusion of inflation-linked products in portfolios.

We are concerned, however, that the exposure draft's proposed inclusion of two disaggregated indices the Bloomberg Ausbond Government 0+ Yr index (Government) and the Bloomberg Ausbond Credit 0+ Yr index (Credit) in the Performance Test dilutes the impact of implementing the Master index for inflation linked bonds.

The Bloomberg AusBond Index Family



As is visible from the chart these disaggregated indices do not include supranational, sovereign, and agency securities (SSA), nor inflation linked bonds.

AFMA understands that if these indices are included as alternative performance benchmarks, uptake of the Master Index is likely to be significantly impacted.

This action if done in isolation could impair trading in AUD denominated inflation linked bonds and SSA securities and impact secondary market liquidity.

If these disaggregated indices are to be included then we suggest that two additional indices also be included so as not to discourage allocation and participation to the supranational, sovereign, agency and inflation linked markets. These would be the Bloomberg AusBond SupraSov 0+ Yr Index (SSA Index) and the Bloomberg AusBond Infl Govt 0+ Yr Index.

The Bloomberg AusBond Infl Govt 0+ Yr Index is engineered to measure the market of inflation-linked bonds issued by the Govt and Semi-Govt Authorities of Australia. A separate Inflation Linked Index is a better choice to measure performance of portfolios containing inflation linked products and would be consistent with the implementation of the Government and Credit indices.

The Bloomberg AusBond SupraSov 0+ Yr Index (SSA Index) is engineered to measure the market of bonds issued by foreign supranational, sovereign and agency (SSA) issuers in Australia. A separate SSA Index is a better choice to measure performance of portfolios containing SSA securities and would be consistent with Treasury's recommendation to use the implementation of the Government and Credit indices for performance measurement.

Inclusion of these indices would provide greater choice for fund managers to benchmark their portfolios against asset classes that include inflation linked bonds and the supranational, sovereign and agency.

Government index free float

We note that approximately 27% of the securities that would be measured by the Government index are held by the RBA and domestic banks due to open market operations, capital adequacy and regulatory capital requirements and liquidity coverage ratio purposes. The Government index is based on the total outstanding amount of AGS and semi-government securities and not the actual free float available introducing risk to fund performance. Fund managers following the Government index will have to consider either purchasing expensive AGS or semi-government securities to track

the index or invest further down the credit spectrum to enhance fund performance. Inclusion of the Bloomberg AusBond SupraSov 0+ Yr Index index would offer a higher-grade alternative tracking option that delivers a better return than lower rated securities as SSAs generally trade at a spread over AGS and semi-government securities.

Conclusion

The exposure draft proposals have the potential to lead to unintended consequences for SSA securities and inflation linked bonds.

AFMA recommends that Treasury adopt benchmark indices that exclusively include inflation linked bonds and SSA securities to measure the performance of fixed income portfolios; specifically,

1. Add the Bloomberg AusBond Infl Gov 0+ Index to the list of approved indices,
2. Add the "Bloomberg AusBond SupraSov 0+ Yr Index" to the list of approved indices.

Yours sincerely,

A handwritten signature in blue ink that reads "Mark McCarthy". The signature is written in a cursive style with a horizontal line underlining the name.

Mark McCarthy
Director for Markets Policy