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The problem with "Big Bucket" super funds in drawdown phase?

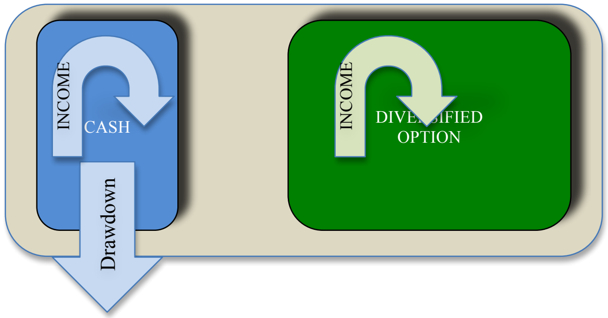
A lot has been written and served up to us through advertising channels about the benefits of the low cost industry super fund network. At A Clear Direction we think that some industry super funds offer a good option for clients especially with low balance beginning their superannuation savings journey.

However, a major issue I have with the "Big Bucket" investment approach offered by these and other superannuation offerings comes to when you want to start drawing down on the balance to sustain your cost of living and lifestyle in retirement.

By Big Bucket approach I mean whereby you have a range of investment choices, which hold a diversified pool of assets, and you get to choose one or two of these choices.

The problem comes once you start to draw down. A few years ago you did not have the choice of targeting where to draw your payments from. This thankfully has improved so now a member could have a cash option and draw all payments from there along with a balanced, moderate or conservative diversified option.

So a suggested structure within these big bucket funds look's like this:



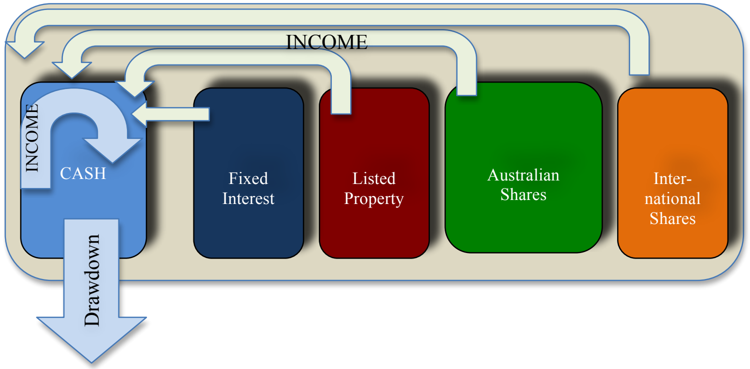
This all sounds pretty reasonable. The problem in the structure is that the investment earnings generated by a particular investment option are not able to be directed back into the cash option to top it up. Rather they get automatically re-invested so you quickly see the cash component dwindle.

So what this means is that a member has to manually sell down assets from the diversified option to top up the cash account. What they are doing is selling a range of asset classes. This includes selling down growth style assets such as shares and property.

If those investments have been steadily growing this is not a problem as we would be undertaking effective rebalancing. Unfortunately when growth asset markets are struggling, selling down these assets is locking in the losses or poor performance that has occurred.

Take the past 5 years as an example. We are still well away from seeing shares and listed property assets regaining the levels of late 2007. If we are forced sellers now we are locking those paper losses into real losses.

In my opinion a much more effective arrangement is to take control of where the income generated by assets is invested and in doing so reducing the need to be forced sellers of assets at a point in time.



Another interesting side issue is to know where administrative fees are being taken from in "Big bucket" accounts. Most likely it is across the investments proportionately. Here is another situation when you can become forced sellers when ideally it would be better not to do so.

At A Clear Direction we believe that you can have the benefits of a low cost superannuation service along with the necessary control to make sure you are not forced into making poor investment decisions along the way.