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House of Representatives Standing Committee on Economics
Inquiry

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House of Representatives Standing Committee on Economics
Inquiry into the Implications of Common Ownership and Capital Concentration in Australia

Prime Super welcomes the opportunity to provide a submission to the House of Representatives Standing Committee on Economics in relation to the Inquiry into the Implications of Common Ownership and Capital Concentration in Australia ('the Inquiry").

The Inquiry has sought comment of the following matters:

- The extent of capital concentration and common ownership of public companies, and its likely future trajectory in Australia;
- The influence of capital concentration and common ownership on markets, including on investment decisions, market behaviour, competition and any other relevant factors;
- The changing influence between individual investors and small funds, compared to larger funds, as a result of capital concentration and common ownership;
- Any related consequences that flow from capital concentration and common ownership, including international experiences;
- The role of regulators in responding to these consequences; and
- Policy responses to address these consequences, including by government, regulators and public companies.

Background

Prime Super is an independent, profit-to-members superannuation fund. We have provided superannuation and retirement solutions to Australians for over 25 years. Today we manage approximately $6.3 billion in retirement savings for around 125,000 members who work in industries including agriculture, horticulture, health, education, aged care and recruitment.

Prime Super makes the following comments in relation to the Inquiry.

General Comment

The concept of a buyout of a public company and the resulting move to a private company is part of an efficient and effective financial system. Such transactions occur where private

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investors see embedded value in a public company that is not fully included in the current share price, or operating nature of a listed Company.

The tension between the business of a public company and a potential take-over from a private entity creates a more efficient capital system, and more effective and efficient management of those companies. Which is in the long term best interest of investors in public companies.

Capital Concentration

The Australian superannuation system has a value that is close to $3.3 trillion whilst the Australian Listed Stock Market is valued at around $2.5 trillion.

APRA statistical data to 30 June 2021 reports for superannuation funds with more than four members that there is over $500 billion invested in Australian Shares, which represents 23% of the superannuation pool. If this is extended to the full superannuation pool of assets (noting that small member funds may indeed have higher or lower allocations to listed shares), then roughly $760 billion in shares is held by superannuation funds, or 30% of the total value of the listed stock market.

The current superannuation system has a large number of small self-managed superannuation funds, plus industry funds, retail funds, public sector and corporate superannuation funds. This diversification of superannuation entities and therefore owners of listed shares supports a broad open market.

The Productivity Commission review of the efficiency and effectiveness of the superannuation system recommended that the number of default superannuation funds should be reduced to a shortlist, with no more than 10 products. Whilst this recommendation has not as yet been legislated the drive across the industry is for mergers, which will inevitably lead to a small number of very large superannuation funds and a large number of small self-managed superannuation funds.

The outcome of this fundamental change to the industry is a very small number of very large superannuation funds, that have a significant stake in the Australian listed markets.

On the back of mandated contributions the superannuation system is growing rapidly. The consultancy firm Deloitte note in their report "Dynamics of the Australian Superannuation System - The next 20 years", dated November 2019, that the Australian Superannuation industry will grow to $10.2 trillion by 2038. The Superannuation sector will clearly be the largest and most dominant force as an investor in Australian listed shares into the future. How this influence translates through a small number of very large shareholders must be better understood.

The associated risk that arises is the risk of "too big to fail" superannuation funds, and the impact of that risk on investors more broadly in Australian listed shares.

Influence of Ownership

The concentration of capital within superannuation may lead to the following outcomes:

1. Increased influence on the behaviour of listed companies through a small group of influential investors (small investors will have little or no say). There are both positive and negative attributes that will be associated with this concentration of influence; and
2. Where there is a shift to passive investing by the significant superannuation funds, there is the risk that this becomes a 'free-ride' for the management of listed companies, as the checks and balances through shareholders oversight are reduced.

The above outcomes are at either end of an extreme where the result on listed markets in general and the balance of shareholders, being individual shareholders as opposed to institutional shareholders may not be best served.

Transparency

Listed companies have a range of reporting requirements that provide for a higher level of transparency in terms of the operations of the business. This transparency does not occur where those companies have been subject to a buyout and become private companies.

The associated risk is that the members of the specific superannuation fund owner may receive a benefit through the improved performance of that one particular company, but the consumer in general will have a sub standard outcome through higher profit taking by the shareholder.

The alignment between the best interests of superannuants and Australian citizens in general may broadly ensure a reasonable outcome. The deferred nature of superannuation means there will be cases where an alignment is not met, the most obvious being a higher cost for products and services during an individuals working aimed which is offset by a greater return for investors and so increases superannuation account balances, which is a clear benefit for those with more financial resources.

International Experience

Morgan Stanley published a report in August 2020 entitled "Public to Private Equity in the United States: A Long-Term Look".

This report notes (page 25) in relation to US public equity companies, that:

> *"There are one-half as many public companies as there were in 1996 and three-quarters as many as there were in 1976.*
>
> ...
>
> *The market capitalization of the U.S. stock market has increased significantly since 1976 despite the decline in the number of listed companies."*

Although the total value of listed markets has increased the number of companies that make up the markets is in decline. This change is attributed to a number of aspects, including:

- the cost and complexity of listing has increased which means a business must be bigger to be a part of the general listed stock market; and
- there is a greater benefit to larger companies to grow through acquisition rather than innovation.

It is likely that Australia will continue to follow the lead of the far bigger US market. Australia already has a very highly concentrated market with the Banks and big miners making up a large portion of the total market.

This then exposes the Australian Stock Market to concentration in both the total number of companies on the market, as well as a concentration in the number (and views of) the shareholders.

Conclusions

There is no concern in principle to a private equity investor buying out shareholders in listed companies. This is good for both the listed company and the private company, and is the sign of a strong economy with an efficient capital cycle.

More in depth analysis is required to better understand the impact on the Australian economy and the Australian consumer in light of:

1. increased consolidation within the Australian superannuation sector;
2. the influence that a highly concentrated investor base will have on the Australian listed stock market;
3. the balance between the immediate interests of consumers and the interests of those consumers at the point of retirement;
4. the change in disclosure that will arise though an increased number of companies moving into the private sphere; and
5. greater understanding on the impact on the Australian listed stock market if more companies move from the public to private sphere, as is evidenced in the United States.

Prime Super would be happy to discuss any aspects of this submission further.

Lachlan Baird
Chief Executive Officer