



Hong Kong
Women Professionals
& Entrepreneurs
Association Limited
香港女工商及專業人員聯會有限公司

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Mandatory Provident Fund Scheme Authority
Investment Regulation Department
Unit 1501A, International Commerce Centre
1 Austin Road West, Kowloon

Dear Sir/Madam

Consultation on Providing Better Investment Solutions for MPF Members

In response to the Consultation on "Providing Better Investment Solutions for MPF Members", members of the Hong Kong Women Professionals & Entrepreneurs Association (HKWPEA) have set up a Task Force to study and discuss the questions contained in the Consultation document.

Attached herewith please find our HKWPEA's response paper to this consultation for your kind perusal. For any further enquiries or information, please do not hesitate to contact us at 2882-2555.

Yours faithfully,

Agnes Koon
Hong Kong Women Professionals & Entrepreneurs Association

Q1. Do you support the direction of introducing a core fund in the manner set out in paragraph 36 (a) to (d) above?

Yes No It depends

Comments:

Generally speaking it is a good idea for the MPFA to provide guidelines as to how default funds should be run, but there are issues that require further consideration – such as the term “Core”, which implies that the fund is the “Center” of the scheme and further misleads members to believe that it is the “best choice” that is structured under the recommendation and guidance by the MPFA. It is considered an extremely high undertaking by the MPFA to aim for the default fund to serve as a default asset allocation that looks to correct behavioural and cognitive biases of members and “correct” the speculative behavior of over-allocation to equities (paragraph 32).

HKWPEA supports the direction only if the methodology and implementation can be practical and transparent enough to meet the objectives it was set out to accomplish. This must be without causing mixed messages for those who are already making proactive selections, as compared to those who are not, which currently stands at a minority rate of less than 24%.

Q2. Do you agree that the CF that is the default fund should be substantially the same in all MPF schemes?

Yes No

Comments:

If default fund were to be implemented, they should be governed by the same sets of principles and guidelines offered by the MPFA, in order to ease providers’ accountability of exercising too much discretion. However, it is challenging to derive a common consensus for an outcome that is “substantially the same” among the different default funds.

Q3. Do you agree that it is appropriate that the core fund be based on a standardized default fund?

Yes No

Comments:

We cannot see how any investment planning can be standardized. The SFC and MPFA have always tried to educate the investment public that they should learn about their own investment risks – including but not limited to time horizon, longevity, perception of risks, and their own situations before taking out any investment decisions.

How could “life cycle” or “target date” be determined across the board? Every member as every individual has a different health condition and medical history such as hereditary risks, etc... Standardization will go against every effort the regulators have tried in the past to educate the public in taking one’s investment responsibilities.

If standardization means low fees across the board, the members might be subject to unnecessary concentration risks and risks due to lack of active management (See response to Q7). **Q4. Do you agree**

that the appropriate investment approach of the core fund is one that automatically reduces risk over time as the member gets closer to age 65? If not, what other option would you propose?

Yes No

Comments:

Absolutely not. Quite on the contrary to a lump sum investment, a regular investment is required to go through different market cycles and volatility to optimize its Internal Rate of Return (IRR), where returns have been risk adjusted.

We do not see how the default fund can automatically reduce risks. Say a member is now 55 and is placed into a default fund (paragraph 45-49) which is classified as a target date fund or life cycle fund. At his current age, he is most likely placed in global equity between 60% and 75%. Unexpectedly the market goes through a bad cycle for the next five years, which according to the plan will see his contributions and/or accrued benefits automatically switched into less risky assets, such as global bonds. His accumulated "units" will be switched at a lower valuation into bonds – something growing at a slower pace. When he retires his portfolio value may be in a worse shape than if he was to stay in the equity markets waiting for a recovery. Ditto to the response for Q3, standardization could be a risk which is placed on the members.

Q5. Do you have any preliminary views on the technical issues set out in paragraph 48, in particular whether consistency is required on all aspects of default fund design in all schemes or can some elements be left to the decision of individual product providers?

Comments:

Automatic derisking is a risky approach and it should not be standardized across the board. Whether it is a default fund or other constituent funds, the objective is to help members diversify their risks within the portfolio across all age groups, and to achieve returns that rise above inflation for capital preservation.

To achieve better diversification there is plenty of room for major improvements on the current CF's structure. The existing asset types are primarily equities and bonds, with equities generally in Hong Kong, Asia, Europe, North America or global. These two asset types have become strongly correlated over the recent years. Asset classes perform differently and have different characteristics across countries and regions and by allowing Emerging Markets' equities and bonds, real estates and commodities will significantly reduce the risks within a portfolio. For example, iShares MSCI Emerging Markets Index has a negative correlation of - 0.12 against the iShares Barclays TIPS Bond Fund. Similarly the SPDR Dow Jones Intl Real Estate has a negative correlation of -0.14 with the iShares Barclays TIPS Bond Fund, over a 1 year period. Allowing more risky asset types would see younger scheme memberstake advantage of the longer time horizon.

We believe it would be best that the MPFA would consider relaxing investment restrictions by allowing more asset classes that are either low in correlation or negatively correlated.

Finally, for the same reason as described in Q2, if a default fund were to be implemented substantially the same in all MPF schemes, providers should not be allowed to have discretion and the MPFA should be ready to undertake any responsibilities that come with the guidelines to be provided for the providers.

Q6. Do you agree that keeping total fee impact for the core fund at or under 0.75% is

a reasonable initial approach?

Yes No

Comments:

We don't believe it is possible to achieve quality with a fee cap of 0.75%, particularly when looking at fees around other asset types including equities, bonds and mixed assets, with their weighted average FER being 1.7%, 1.47% and mixed assets at 1.83% respectively. At this current AUM level, under most providers the proposed fee scale is highly unlikely to be achievable unless a passive strategy, i.e. a tracker fund, is to be implemented.

Given the current restrictions of the CF structure, it is extremely difficult if not impossible to find an existing benchmark that would measure up to the requirement. If a new benchmark is to be established by each provider, it may not be scaleable for the relatively smaller trustees – making it a non-level playing field for smaller providers.

The tracker will lack flexibility and will not achieve the purpose, as described in paragraph 32, of attaining the most optimal strategic asset allocation. In addition, it is also the authority's objective to reduce risk with this default fund. It is suspected that low tracking errors are to be expected of providers – this will cancel out all advantages of investing in a regular mode.

If the MPFA considers funds with FER 1.30% or lower as low-cost funds, we do not understand why there needs to be pressure on the providers to go far below this figure. This will send the wrong signal to members that the fee is the most important consideration in MPF management. Shall this default fund become too popular due to its low fees, most members will be entering into an overly concentrated tracker, including those who might have already been making proactive decisions.

It would be more appropriate for the fund to start with a minimum FER 1.30% , with the fee being reviewed in 3 years' time.

Q7. Do you agree that keeping total expense impact (i.e. FER) for the core fund at or under 1.0% over the medium term is a reasonable approach?

Yes No

Comments:

Due to the reasons mentioned in Q6, it is not a level playing field for smaller players to be achieving an AUM as they do not have the same customer base as other bigger providers, such as AIA or HSBC, or direct fund providers such as Invesco or Fidelity.

Therefore, as mentioned, it would be ideal for the fund to start with a minimum FER 1.30% and to review the fee in 3 years' time. If this default fund is to be substantially the same between providers, rather than capping the maximum fee, it is best to set a minimum fee with an upper cap to avoid extreme cut-throat competition. Bear in mind that this is a default fund that was meant to care for the ones who have opted not to choose, and a fund equivalent to other CFs on the schemes offered by different providers.

Q8. Do you agree that passive, index based, investment strategies should be the predominant investment approach in the MPF core fund?

Yes No

Comments:

No. For the same reason as specified in Q4 and Q6, the tracker will lack flexibility and will not achieve the purpose as described in paragraph 32 of achieving the most optimal strategic asset allocation. In addition, it is also the authority's objective to reduce risk with this default fund. It is suspected that low tracking errors are to be expected of providers -- this will cancel out all advantages of investing in a regular mode, in which returns have been risk-adjusted on a monthly basis. Also it is unlikely for an index to be in existence that would satisfy the current MPF structure and therefore one would have to be created.

Q9. Are there particular asset classes which you think would not appropriately be invested on a passive, index based approach?

Comments:

Asset classes that are more complicated to understand, or assets types that bear undue risks such as managed futures, derivatives, high yield debts, etc..should be avoided.

Q10. Do you agree that the name of the core fund should be standardized across schemes? If so, do you have any preference amongst the possibilities set out in paragraph 77 above?

Yes No

Your preference:

"MPF Core Fund" (having regard to its use as a core investment approach for retirement savings)

"MPF Basic Investment Fund" (emphasizing its design as a basic investment approach for retirement savings)

"MPF Simple Investment Fund" (emphasizing its design as a simple investment process for retirement savings)

"MPF Default Investment Fund" (reinforcing that its primary design is built around the default investment strategy for those who do not, or do not want to make an investment choice in saving for retirement)

"MPF "A" Investment Fund" (or some other term which removes any implications about the nature of the strategy)

Comments:

As mentioned, we do not agree with the fund to be referred to as the "Core Fund" due to reasons as specified in Q1.

Q11. Do you agree with the general principle for dealing with implementation and transitional issues as set out in paragraphs 78 and 79?

Yes No

Comments:

In principle, shall this become enforceable by law, accrued benefits could be switched from the existing default fund of a scheme to the new default fund of that scheme. Anyway a member can also choose to move his/her MPF benefits to any other MPF scheme in the market.

Q12. Do you agree with the proposal in paragraph 81 as to how to deal with the transition for existing MPF members of default funds?

Yes No

Comments:

The MPFA should give clear guidelines for providers and this has to be dealt carefully with a public gazette process, clearly defining actions for members who could not be found. Members should be given an opportunity to select their investment when a transition is made, with marketing pamphlets clearly describing the pros and cons of selecting to choose and selecting not to choose an investment choice.