

## **Final report for the AFAANZ grant received for 2017-2018**

### **(1) Name, Position, Contact Details for each applicant**

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### **(2) Project Title**

Information Costs and Superannuation Choices in Australia

### **(3) Updated Project Summary (500 words) including any variations between the project undertaken and the original application**

Recent years have seen an international trend towards the adoption of simplified short-form disclosure documents for retail financial products (Godwin & Ramsay 2014, 2016). For example, regulators in the United States and Europe have corseted retail investment disclosures into a few pages of strictly controlled information (European Commission 2009, 2012; Securities Exchange Commission 2007). In Australia, the “short Product Disclosure (PDS) regime” was introduced in 2011 to make superannuation product disclosure shorter and simpler and assist retail investors with informed investment decision making. Since these regulatory changes were introduced, not much is known about the current disclosure practice of retirement saving funds and its impact on member choice. Therefore, this study provides an exploratory analysis of the standard short superannuation PDS by using two dimensions of disclosure quality (1) readability and (2) content. Additionally, arguments regarding managerial disclosure incentive are also tested to determine whether performance affects funds’ strategic use of PDS disclosure. Finally, we examine whether quality PDS disclosure facilitates investor choice in Australia, i.e., whether the readability and extent of PDS

disclosure are associated with observable investment flows.

The provision of information typically can provide important consumer benefits such as improved decision making, enhanced product quality, and lower prices (Mazis et al. 1981). However, in order for that information to have a positive impact on member's decision-making process, the information must be easily accessible and presented in a clear and understandable format. Useful information that helps reduce information interpretation costs needs to (1) be presented in an easy-to-understand manner, and (2) contain all important information that are most relevant to investors. Hence, both the **readability** and **content** of PDS disclosure are examined in the Australian retirement saving setting.

This is the first study that investigates the attributes of a large sample of Australian retirement saving fund PDSs in a systematic fashion. Much of the literature on fund disclosure has relied on the research methodology of experiments to manipulate the content and format of the information disclosed and used qualitative methods to document key themes and provide insights for follow-on studies (Bateman et al. 2016; Bateman et al. 2015; Beshears et al. 2009; Cheah et al. 2015; Foster, Ng & Wee 2015; Kozup, Howlett & Pagano 2008). In comparison, this paper uses the actual disclosure documents and quantifies the extent and readability of information contained in PDS documents by using both an objective computational linguistic readability measure and subjective content analysis measure. The resulting disclosure scores are then used to explore the relationship between fund disclosure and members' choices. This approach also distinguishes this study from previous fund studies that use various fund characteristics related to fund visibility (e.g., fund size, loading or expense ratio) to indirectly proxy for the reduction in information costs. To our knowledge, there has been no direct empirical investigation of how the short PDS affects members' choices, even though the effectiveness of the new short PDS in helping investors select funds should be a fundamental and important question for regulators and investors. The results carry important implications with regards to the current and contentious issue of retirement saving fund's disclosure's transparency and informativeness. Moreover, our study adds to the understanding of the global trend towards the adoption of short-form disclosure documents for retail financial products by showing whether the use of short-form disclosure document is merely a compliance and liability minimization exercise, or indeed a useful mechanism to provide important basic information and attract potential investors.

#### **(4) Funds Granted**

\$5,000

**(5) Detailed Report on Expenditure of Funds against Budget Items, with variations explained**

Research assistants are engaged to collect and update superannuation PDS data and score the PDS content. The cost is based on the hourly rate of \$43.71 for academic casual staff at UQ in 2017. A total of \$7,650 was requested at application. Nevertheless, the authors spent their own time on part of the data collection and cleaning work and have all the work completed.

**(6) Outcomes, for example, working papers, presentations and publications (give full details, including abstracts)**

- 1) Completed working paper titled “Simplified Retail Financial Products Disclosure and Investor Choice: Evidence from Australian Retirement Saving Funds” (see attachment)
- 2) Presentations at
  - a. UQ Accounting research day, February, 2018
  - b. FIRN annual conference, November, 2018

**(7) Future Intentions for this Project (give full details)**

**Journal submissions**

- 1) Submission to an ABDC-A accounting and finance journal
- 2) UQ New Staff Research Grant

**(8) Summary of Outcomes and Benefits**

This study examines the current Australian retirement saving plan PDS disclosure practice as reflected in PDS readability and quality under the new short form regime given the importance of effective PDS disclosure for investment decisions. These issues are important given the serious concerns raised by regulators about the usefulness and understandability of fund PDS disclosure, which resulted in the introduction of the short form PDS regime in 2011 to make it

easier for fund investors to locate important information in the PDS and compare information across retirement saving products (ASIC, 2011).

This is the first empirical investigation of retirement saving investor PDS. Specifically, the lexical feature of the PDSs and the extent of detailed reporting in the PDSs are examined using computational readability scores and content analysis index. The results show that the overall reading ease of the PDSs analysed are classified as either “ideal” (which is less readable than “acceptable”) or “fairly difficult to read” based on commonly used readability measures. On average, industry funds provide better PDSs as opposed to their retail counterparts, in terms of both readability and the extent of disclosure. Since the short PDSs were first introduced, retail plans PDSs are found to have deteriorated in terms of both readability and content from 2012 to 2013 when the Short PDS Regime was first introduced. The readability of retail funds PDSs then improved slightly from 2013 to 2015. Industry funds’ PDSs have improved in both dimensions of readability and content, except the Flesch score which deteriorated slightly over time for industry funds. Nevertheless, a trend worth noting is that retirement saving funds PDSs are becoming increasingly alike, as indicated by decreasing variation in the two disclosure measures for the PDSs. Contrary to the “management obfuscation hypothesis” or “good news hypothesis”, we find no significant relation between fund’s performance and the readability and extent of PDS disclosure.

This study also provides empirical evidence on the fund flow consequence of PDS disclosure properties using the linguistic properties of fund PDSs. More specifically, we study the implications of the readability and extent of PDS disclosure for investment inflows. The empirical findings can be summarized as follows. First, retirement saving funds provide more readable PDSs when there are more inflows, but there is only weak evidence for the overall sample that investors are attracted to plans because of the ease of reading of PDSs. One possible reason is that the overall PDSs are already relatively easy to understand under the short-form PDS regime. Second, our results show that more inflows encourage funds to provide more and better information in the PDS, especially the industry funds. In support of Hypothesis 4, the quality and extent of PDS disclosure is positively associated with fund inflows. This relation is especially strong for the retail funds. Viewed collectively, this provides important evidence that retirement saving funds with better PDS content do attract more inflows.

The results from this study provide insights into the strategy to be pursued by different types of retirement saving funds, regulation formulation to guide and encourage

informative and understandable PDS disclosure. Moreover, it adds to the literature of retirement savings and more generally, the literature of managed funds, by providing empirical evidence in addition to experimental study evidence and inferences drawn from survey or focus groups with respect to investors' long-term saving arrangements.

Given the complexity of investors' financial planning problems and the often confusing financial products that are offered to them, potential remedies can be provided to reduce the incidence of investment mistakes and welfare costs, such as consumer regulation, disclosure rules and financial education (Campbell 2006). Therefore, our study on retirement saving funds PDS disclosure and investment choice offers a practical rationale and empirical evidence for future study of retail investor behaviours.