

Treasury Review of the Superannuation Performance Test

Submission by Quest Asset Partners June 2026

Executive Summary

Quest Asset Partners welcomes the Treasury’s review of the superannuation performance test. We are an active Australian equities manager with the highest possible ratings from WTW, JANA and Lonsec, and two decades of adding value to equity portfolios. While we are not a superannuation provider, our daily presence in Australian equity markets gives us a direct line of sight to how regulatory settings are shaping investor behaviour — and where that behaviour is causing harm.

Our central argument is this: the performance test has created powerful regulatory incentives for superannuation funds to hug the ASX benchmark index. This is distorting the index itself, amplifying market volatility, inflating valuations across the largest ASX constituents, and — most importantly — reducing the long-term returns available to retirees.

We support Option 2, with a material variation: the ASX 300 should not serve as the benchmark. We propose a peer-relative, risk-adjusted framework, described in Section 6, that better serves retirees and the integrity of Australian capital markets.

Statements for Media Use

The following statements summarise our core concerns and are intended for use in media coverage of this submission.

“We see the cracks in the base of a major dam, and much of Australia is downstream. The performance test was designed to protect retirees — but by forcing superannuation funds to hug the ASX index, it has set in motion distortions in our capital markets that will harm retirees and the Australian economy for decades if not addressed.”

Quest Asset Partners, Submission to Treasury, June 2026

“The ASX is open six hours a day, but 30% of all trades now happen at exactly 4:10pm. That is not a market engaged in price discovery — it is a market organised around index mechanics. The performance test created this, and it will keep getting worse as superannuation assets grow.”

Quest Asset Partners, Submission to Treasury, June 2026



“Major index weighted stocks are trading well above their history, their global peers and the balance of the ASX. These valuations are not justifiable by EPS growth or EPS revisions. The Superannuation performance test is largely responsible. ASX index is now simultaneously a benchmark, a target and a distortion. Change is necessary.”

Quest Asset Partners, Submission to Treasury, June 2026

1. A Structural Shift to Index Hugging

Until recently, most major superannuation funds outsourced their Australian equities allocations to active investment managers. This reflected a long, consistent history of the median Australian equity manager adding value over the index – with the ASX index itself historically ranking in the third quartile of manager performance or lower.

That picture has changed dramatically. The index return has moved from the third quartile to the first quartile of manager performance – see section 4 below. One explanation is that active managers have suddenly and collectively lost their skill. The more credible explanation is that the regulatory environment has altered the behaviour of a large portion of the market in a way that has shifted the index itself.

The performance test has made deviation from the ASX benchmark a direct source of regulatory risk. We have heard directly from clients who are choosing to hug the index not to maximise member returns, but – and we quote - ‘to avoid benchmark variance’, whether positive or negative. The Consultation Paper notes this risk but frames it as a stakeholder ‘suggestion.’ It is not a suggestion. It is the observable, documented consequence of a test that treats underperformance relative to the index as regulatory failure, regardless of the absolute return delivered to members. The incentive to outperform is much lower than the risk of underperforming.

Industry acknowledgement

- Frontier Advisors has confirmed that active management and allocations to higher tracking error are now ‘direct sources of regulatory risk’ under the YFYS performance test – ‘particularly over short time periods’ (*Pensions & Investments*, July 2022).
- AustralianSuper’s own submission to Treasury in 2023 stated that the proposed changes to the performance test ‘do not address the ongoing risk of funds hugging the benchmark.’
- Macquarie Group’s February 2026 Operational Briefing (Slide 35) documented the material growth in ‘active quant’ mandates – near-index strategies that are among the direct beneficiaries of flows away from true active management.

The shift is also visible in how index constituents are priced. As outlined in Section 2, the largest ASX companies are now trading at valuations that have become detached from their underlying fundamentals – a direct consequence of capital flows that are driven by index weight rather than investment merit. Passive investing is enhanced by the same regulation.

2. The Benchmark Is Now Distorting the Market It Measures

The performance test was designed on the premise that the ASX index is a neutral, objective measure of market performance. That premise requires the index to reflect the independent



judgements of a diverse pool of investors engaging in genuine price discovery. It no longer does.

When a large and growing portion of Australia’s investable capital is required by regulation to track the index, the index becomes self-referential: the benchmark distorts the behaviour it is supposed to measure, and the tool begins measuring itself. We present three streams of observable evidence for this conclusion.

2a. The closing auction: passive flows are reshaping market structure

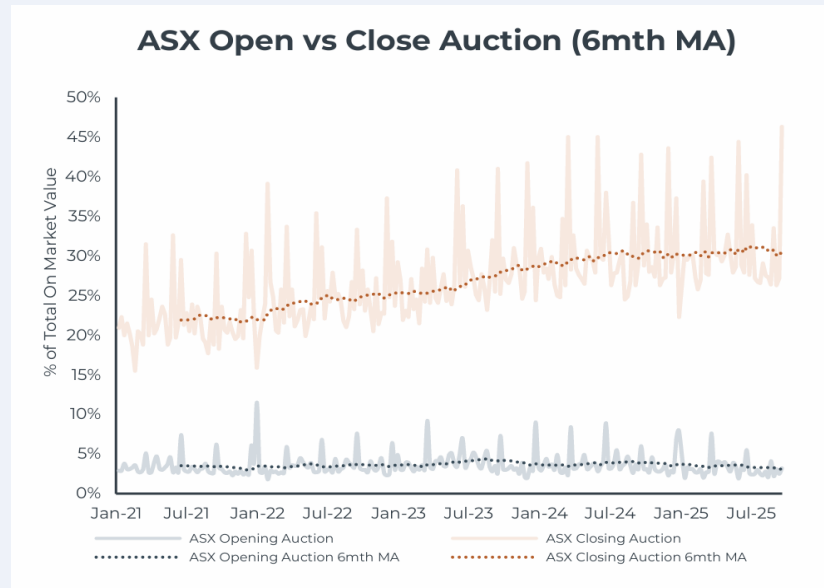
The most direct evidence of the rise of index-tracking capital is the concentration of trades in the ASX closing single price auction at 4:10pm each trading day. Passive¹ investors transact at the official closing index price to minimise tracking error; they have no incentive to engage in intraday price discovery.

Iress data shows that end-of-day auction flows have risen approximately 50% over five years. The ASX is open six hours each weekday, but up to 45% of all trades now occur at the single moment of 4:10pm. The ASX itself has acknowledged the pressure by introducing a new post-close trading session specifically to manage the liquidity volume concentrated in the closing auction, which it noted ‘currently represents over 20% of the entire day’s liquidity.’

Data: End-of-day auction concentration

- End-of-day auction flows on the ASX have risen approximately 50% over the past five years. Approximately 30% of all ASX daily trades now occur at exactly 4:10pm – the closing single price auction. The ASX has formally acknowledged that closing auction transactions represent over 20% of the entire day’s liquidity and has restructured its trading hours in response.

Chart 1: ASX start and end-of-day auction volume trend, 2019–2025, Source: Iress



An exchange that concentrates up to 45% of its daily volume into a single match is not engaged in continuous, value-based price formation. It is a market structurally organised around index mechanics.

¹ The passive cohort includes many ETFs, as well as low tracking error and enhanced index strategies.



2b. Index reconstitution events: extreme volume spikes confirm passive dominance

A second and highly visible indicator of passive dominance is the volume and price behaviour around changes to index constituent weights. When a company enters or leaves the index, or when its weighting changes, passive and near-passive funds must trade regardless of price or value.

A review of the last three years of index changes reveals some remarkable share register adjustments relating to index changes. The table below, drawn from ASX data, documents the instances where an index change resulting in more than 10% of a company's shares traded on that day. The table is more ASX listed companies with a market capitalisation greater than \$5bn. The highest adjustment Quest has recently observed was a combined ASX 200 and FTSE index adjustment where 19.5% of Genesis Minerals (GMD) shares changed hands on 15th September 2023.

Data: Index reconstitution volume spikes (Sources: Quest / Dimensional Fund Advisors 2025)

- A 2025 global study by Dimensional Fund Advisors found that ASX 300 trading volumes can spike to up to 149 times normal levels on reconstitution days — making the ASX 300 one of the most volatile indices globally at rebalancing, among all major non-US benchmarks studied. Dimensional found this creates meaningful and measurable trading costs for index-tracking funds, driven by forced trading in the closing auction when prices are most distorted.
- Quest has compiled the following table from ASX data, detailing the ten large market cap register adjustments associated with Index changes over the last three years.²

Largest single-day rebalance turnover, ASX 200, market cap > A\$5bn, last 3 years

#	Company	ASX Ticker	Rebalance date	Event	% of Mkt Cap
1	IGO Ltd	IGO	29-Feb-2024	MSCI Feb review (results same week)	14.6%
2	Pilbara Minerals	PLS	29-May-2026	MSCI May review	14.3%
3	Aurizon	AZJ	30-Aug-2024	MSCI Aug review	12.8%
4	GPT Group	GPT	30-May-2025	MSCI May review	13.6%
5	Orica	ORI	28-Feb-2025	MSCI Feb review	12.4%
6	Evolution Mining	EVN	30-May-2025	MSCI May review	12.2%
7	Mirvac	MGR	28-Feb-2025	MSCI Feb review	11.6%
8	Treasury Wine Estates	TWE	30-May-2025	MSCI May review	11.9%
9	Seek	SEK	28-Feb-2025	MSCI Feb review	11.6%
10	Ramellius Resources	RMS	19-Sep-2025	S&P/ASX + FTSE review	10.2%

An Index Analyst has become one of the most significant sources of alpha — and risk — in Australian equity portfolios. This is a direct consequence of the volume of capital now obligated to respond to index changes rather than company fundamentals.

2c. CBA and the benchmark valuation bubble

Perhaps the most consequential evidence of benchmark distortion is the valuation of Commonwealth Bank of Australia (CBA) — Australia's largest company and recently the single

² Using only ASX Index changes also reveals material register adjustments associated with an index change but to a lower effect. These studies don't include material trading volumes in the period leading to actual date of change.



largest constituent of the domestic equity index. Our previous submission argued that APRA-related flows were responsible for Australian banks being among the most expensive in the world relative to global peers.

We also acknowledge an additional factor: the number of Australian companies included in the MSCI World Index began shrinking in 2020. As a result, the average market capitalisation of the remaining ASX constituents in the MSCI rose 2.2 times — materially more than can be explained by either the reduction in the number of companies or underlying earnings growth. 2020 was also the year in which CBA's PE rating began its ascent toward extreme valuation territory.

CBA is not alone. Some of Australia's largest index constituents — major banks, telcos and supermarkets — are now among the most expensive companies in the world in their respective categories. Index investing in these stocks has recently produced strong returns, but it increasingly resembles what it is: a valuation-agnostic accumulation of large, expensive, incumbent businesses funded by regulatory compulsion.

3. Volatility Has Reached Levels Previously Seen Only in Crises

The displacement of active investors by passive and near-passive capital has materially increased volatility in Australian equity markets. Active investors serve a stabilising function: they buy when momentum pushes prices below fair value, sell when it pushes them above, and provide liquidity when passive funds need to adjust positions. As active management has been crowded out, this stabilising force has diminished.

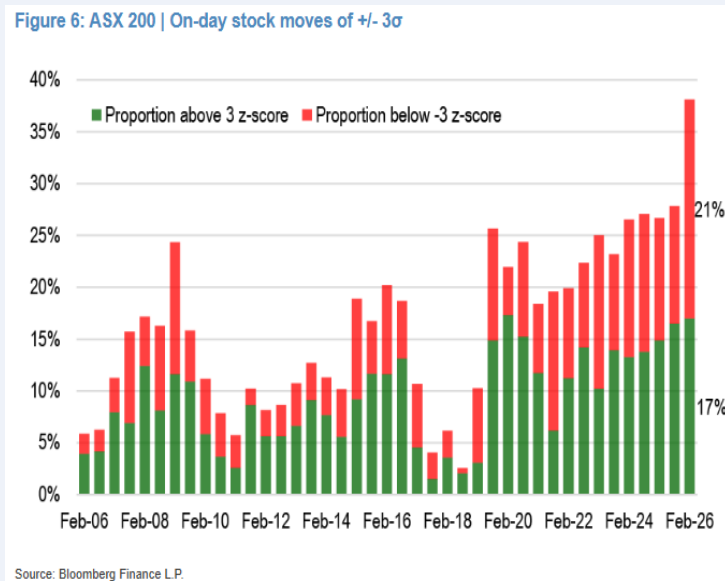
The most visible consequence is in the distribution of share price moves on company results days — the moments when fundamental information is most available and markets should be functioning at their most efficiently.

Data: Results-day volatility (Sources: JPMorgan / Morningstar / AFR)

- A JPMorgan analysis of ASX 200 results-day share price moves over 20 years shows that volatility since 2022 has become 'remarkable' — with moves that were previously associated with the GFC now representing average outcomes.
- August 2025 was the most volatile ASX reporting season in at least a decade, as measured by average share price moves on results day (Morningstar, March 2026).
- February 2026 was described by Morningstar as only marginally less volatile — covered stocks moved an average of 5% on results day.
- Multiple brokers, measuring this independently, reach the same conclusion: price reactions to company results are now materially larger than any comparable period outside the GFC. A three-standard-deviation share price move on a results day — once an exceptional event — is now commonplace.
- The AFR's coverage of the most recent reporting season documented the same pattern: *'Enshittification of ASX is no joke, Something vital may be breaking'*, 27th Feb 2026



Chart 2 JPMorgan results-day move distribution, ASX 200, 2005–2025



The cost of equity is rising. Higher and less predictable share price volatility increases the risk premium that companies must offer to attract capital. This is a tax on Australian business investment that compounds over time and has no direct visible line item on any budget — making it easy to overlook, but no less real.

We have also been advised that results-day volatility is creating genuine boardroom tension. Directors are questioning executives about share price moves that appear disproportionate to the information disclosed. This is damaging to the relationship between listed companies and their management, and to the quality of investor-company engagement more broadly. Separately, passive shareholders — now majority holders in many ASX companies — are unable to provide views on takeover bids or strategic decisions: they hold solely in reference to index weight, with no interest in the underlying business.

4. Retiree Returns Are Being Reduced

The stated purpose of the performance test is to protect retirees from poor fund performance. We support that objective without reservation. But the current design is generating a different harm to retirees — one that is less visible but potentially larger in aggregate impact.

By suppressing active management across a \$4.5 trillion system (APRA, December 2025), the performance test is reducing the pool of available long-term returns. The superannuation sector allocates approximately 23% of total assets to Australian equities. A structural reduction in the return available from that allocation — caused by regulatory incentives rather than manager failure — is a real and growing cost to members.

The unquantified cost to retirees

- The Consultation Paper does not appear to have quantified the return cost of the regulatory suppression of active management. A strong incentive to reduce risk also reduces return. We believe this analysis is essential.



- Historically, the median active Australian equities manager outperformed the index; the index sat in the third quartile of manager results as seen in earlier performance tables.³
- Today, as documented by multiple independent analysts, that relationship has inverted — a reversal that aligns precisely with the introduction of the YFYS performance test.
- If the structural suppression of active management costs retirees 1% per annum in foregone returns, the impact across the 17 million Australians with superannuation accounts, compounded over a working life, is very large.
- The performance test was designed to remove the cost of poor management. Treasury should also quantify the cost of removing good management.

There is an additional and more acute risk embedded in the current composition of the index. Australia's largest index constituents — particularly the major banks — are trading at valuations that are difficult to justify on fundamental grounds. CBA's PE peaked at 31x in June 2025. The financial sector contributed approximately 80% of the ASX's total return in 2024, almost entirely through valuation expansion rather than earnings growth. Members whose funds are compelled to hold these stocks at index weight face significant concentration risk when valuations normalise — a risk that does not appear in any short-term performance comparison.

5. The Damage Extends to Australian Capital Markets

The harm from index hugging is not confined to superannuation member returns. It extends to the functioning of Australian capital markets and, through those markets, to the broader economy.

5a. Reduced equity funding for new and growing businesses

Passive capital is by definition size-driven and valuation-agnostic. It allocates in proportion to existing market capitalisation. Companies must be large enough — and already listed — to attract superannuation capital under a passive regime. This creates a structural gap in funding for smaller and earlier-stage businesses, which are our primary source of new employment and economic innovation. Australia's Top 10 have an average age of 121 years whilst the S&P 500 average is 39 years.

Equity Capital Markets teams have reported to Quest directly that the reduction in fundamental price discovery by institutional investors is a contributing factor to the slump in Australian IPO activity. When there are fewer investors willing to form independent views on the value of an unlisted or newly listed business, the confidence to price and distribute a new issue diminishes.

Data: ASX IPO market (Sources: ASX Capital Markets Reviews 2024 – 2025; HLB Mann Judd IPO Watch 2025)

- ASX IPO capital raised fell from a five-year average of \$5.4 billion across approximately 120 listings per year to just \$1.1 billion across 45 listings in 2023. 2024 saw only 29 new listings — the lowest listing count in two decades — although capital raised recovered partially to \$4.1 billion, assisted by several large transactions.

³ Morningstar Australian Institutional Sector Survey – June 2023 shows the 50th Percentile of Active Australian Equity Manager returns was 9.7% pa for the ten yrs to 30 June 2023. The Index return for the same period was 8.7% pa. The 25th Percentile return was 2.3% pa ahead of the Index over the same period.



- The structural picture is one of a primary market that is raising less capital from fewer companies than the historical norm, in an economy where new business formation and growth require equity funding. The number of IPOs in 2025 rose relative to 2024 but was still well down on historic averages.

5b. The ASX as economic infrastructure

Australia's listed equity market is not simply a trading venue. It is economic infrastructure: the primary mechanism by which businesses access long-term growth capital, and by which Australian savers participate in business ownership. Decades of active capital allocation through the ASX have funded the businesses that employ Australians and generate the income that flows into superannuation.

Index hugging does not destroy this infrastructure overnight. But it gradually hollows it out. As the superannuation sector continues to grow — the RBA projects total assets reaching \$8.1 trillion by 2035 — the share of ASX ownership held by index-constrained capital will continue to rise. Unless the regulatory settings change, the distortions described in this submission will compound.

Australia's economic response to the GFC was materially assisted by the depth and flexibility of its superannuation system — which could direct capital beyond rigid index weights. A system that is structurally committed to holding companies in proportion to their market capitalisation loses that flexibility. It recycles capital into the largest incumbent businesses while starving new entrants of funding. This has material implications for Australian employment and economic dynamism for decades ahead.

6. A Proposed Variation to Option 2

We support Option 2 as a meaningful improvement on the current framework. However, we do not support any Option 2 design that retains the ASX 300 as the reference benchmark. For the reasons set out in this submission, the ASX 300 index is no longer a neutral measure of Australian equity market performance. It is being shaped by the very regulatory incentives the test is designed to evaluate. Using it as a benchmark is circular.

The proposed framework: peer-relative, risk-adjusted performance assessment

We propose replacing the ASX benchmark with a framework modelled on the methodology already used by professional investment consultants — including WTW, JANA and Lonsec — when evaluating active investment managers. It is also consistent with the Information Ratio framework referenced in Figure 1 on page 17 of the Consultation Paper.

The framework could operate as follows:

- Superannuation funds would be grouped into risk buckets based on their historical portfolio volatility — for example, five buckets graduated from low to high risk.
- Fund returns, net or gross of fees, would be compared within each risk bucket against the returns of peer funds with similar risk profiles over a rolling multi-year period.
- Funds whose returns fall into the bottom quartile of their risk bucket would be flagged for scrutiny, with escalating consequences for persistent underperformers.

This approach measures what matters to members: risk-adjusted returns relative to peers operating under comparable constraints. It removes the ASX index from the centre of the assessment and therefore removes the regulatory incentive to hug it. It is already the basis on which the investment management industry evaluates itself — there is no need to invent new methodology.



Importantly, this framework does not disadvantage funds with genuinely good active management. A fund that takes more risk to generate higher returns will be compared to other funds in the same risk bucket — not penalised for tracking error relative to a benchmark it has no obligation to hug.

Conclusion

The performance test has achieved its primary goal: it has drawn attention to genuinely underperforming superannuation products and created accountability where none previously existed. We do not dispute that objective.

But the test has also introduced a significant unintended consequence. By anchoring performance assessment to the ASX index, it has created incentives that are distorting the index, amplifying market volatility, inflating valuations across the largest ASX constituents, and reducing the long-term returns available to the retirees it was designed to protect.

The evidence is specific and observable. End-of-day auction flows have risen approximately 50% over five years, with 30% of all ASX trades now occurring at 4:10pm. Index reconstitution trading volumes spike to 149 times normal levels on rebalancing days. CBA's PE ratio nearly doubled between 2022 and 2025 while its return on equity declined. Reporting season share price moves are at their most volatile in at least a decade. IPO listing volumes in 2024 were the lowest in twenty years.

These are not abstractions. They are the measurable consequences of regulatory settings that have made the ASX index simultaneously a benchmark, a target and a distortion. We urge Treasury to adopt Option 2 with the peer-relative variation proposed in Section 6. Removing the ASX index from the centre of the performance test is the single reform most likely to restore genuine price discovery, reduce structural market risk, and deliver better long-term outcomes for **the 17 million Australians saving for retirement.**

Michael Evans, Director, Quest Asset Partners, June 2026