FROM THE *Managing Editor*

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In this final issue of *JASSA* for 2012 we are fortunate to be able to publish an edited version of the address which Nobel Laureate Professor Robert Merton gave at a recent Finsia conference addressing the topic of optimal design of superannuation. One of the contributed papers also considers superannuation while the other three contributed papers focus on the role of information and efficiency of financial markets.

Also included are three articles which are edited versions of papers presented at the 17th Melbourne Money and Finance Conference — Recent Developments in Financial Regulation: An Assessment — held in July 2012. The conference was organised by the Australian Centre for Financial Studies and kindly sponsored by APRA, the Reserve Bank and Finsia. While not subject to the usual double-blind review process, each of these papers has been reviewed by the Managing Editor and a member of the Editorial Board prior to inclusion.

Professor Robert Merton provides a blueprint for a new, fully integrated retirement system. He argues that the focus should be shifted from wealth available at retirement to the potential retirement income stream which will be available. The strategy of fund managers would be to 'maximise the prospects of achieving a desired standard of living, subject to a risk constraint of a "minimum or essential life income" amount in retirement'. Those parameters can be determined with reference to individual circumstances and preferences, with individuals being made aware of contributions required, and advised regularly on risks of shortfall and adjustments required to contribution rates. Crucially, the complex asset allocation issues involved in achieving the objectives could be 'kept under the hood' — as something which fund managers need to attend to, but which are matters that members have little interest or expertise in.

In the first of the three papers addressing information and efficiency issues in financial markets, Camille Schmidt, Lucy Zhao and Chris Terry focus upon whether changes in the composition of the S&P/ASX 200 Index (over the period 2000 to 2009) have consequences for the returns on shares in companies which are included or excluded. Since this is purely a result of changes in relative market capitalisation of the companies involved, and conveys no new information about their past or future performance, there should be no effect. However, prior studies of index composition change have found evidence of abnormal returns around the event date. These effects are generally attributed to the need for index-tracking funds to rebalance their portfolio allocations (selling shares in those excluded and buying shares in those included) which could directly affect share prices and create trading opportunities for those anticipating such events. Schmidt et al. find no abnormal returns prior to the announcement date, but find that between the announcement date and implementation date, those stocks added had cumulative abnormal returns of 6 per cent which, consistent with cessation of rebalancing trading, were largely reversed over the next month.

Next, Andrew Ainsworth and Jiri Svec examine whether the level and dispersion of one-year-ahead stock price targets of equity analysts help explain the pricing of Australian credit default swap (CDS) spreads. Their results indicate that the level and dispersion of analysts' price forecasts (relative to current stock price), which are interpreted as a proxy for firm cash flow uncertainty, increases CDS spreads. During the financial crisis, equity-based market variables are more relevant to the pricing of CDS spreads than commonly used leverage and credit ratings.

Using McQueen and Thorley's (1994) duration dependence technique, Gilbert V. Nartea and Brett D. Ward examine whether the Australian share market was characterised by rational speculative bubbles over the period from 1985 to 2012. Although previous studies have reported evidence of bubbles in the Australian equity market during the 1987 crash, and anecdotal evidence seems to suggest a bubble episode during the period leading up to the global financial crisis (GFC) of 2009, they find at best marginal evidence of the presence of rational speculative bubbles in the Australian stock market over the period examined.

Returning to the topic of superannuation, Lakshman A. Alles F Fin addresses the issue of sustainable (consumption) withdrawal rates from an initial retirement balance during retirement and the risks of financial ruin. He raises the important question of how retirees can determine the optimal amount to withdraw while maintaining some minimum safety level in their portfolio value if investment returns and remaining life span are uncertain. He notes that financial planners and advisors should pay more attention to the estimation of risk in retirement finance modelling in their analyses and in their advice to clients, and his paper provides some useful guidance on the application of simulation and analytical techniques in this regard.

In the first of the papers from the 17th Melbourne Money and Finance Conference, the paper by Ros Grady on consumer protection in the financial sector indicates that new international principles and standards in this area lack cohesion and leave a number of important issues unanswered. Grady indicates that although significant work has been undertaken to bolster the rules on consumer protection as they apply to financial products and services, there is still much more to be done to determine whether we are addressing the right issues and in the most effective way.

While the full extent and timing of the proposed changes in the regulation and structure of the Australian over-the-counter (OTC) derivatives market are still subject to further consultation, David Robinson SA Fin and Jane Hronsky explore the implications of these proposals. They suggest that the broad intentions of the proposed framework are beginning to emerge: to increase the transparency of OTC transactions and reduce counterparty credit risk, and thereby reduce systemic risk. They also indicate that the proposed benefits of this new institutional framework need to be considered relative to their potential costs.

Finally, Bart Frijns SA Fin, Aaron Gilbert and Alireza Tourani-Rad F Fin assess the market impact of two consecutive changes in insider trading regulation in New Zealand in the past decade, discussing the findings of two of their recent studies and the way forward. The authors suggest that while many countries have taken what appears to be a tough stance on insider trading, treating it as a criminal offence, and that this approach is often very popular with the general public, there is little evidence that these laws are effective.

We sincerely thank all of the authors who have submitted articles to *JASSA* this year and look forward to your comments and more outstanding contributions next year. ■

JASSA articles

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