Trust, Investments and Growth

The perspective from European savers and individual investors

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Abstract

Trust, investments and growth are the key words selected by CONSOB for the event around its new report on

These are also key words for the Capital Markets Union (CMU) initiative that is a priority for European Authorities and that Better Finance, the European Federation of Investors and financial Services Users, strongly supports. Indeed, the CONSOB report for Italian savers, as well as European –wide statistics, show that EU households financial savings are moving ever farther away from the real economy assets in which their funds are invested:

- direct holdings in equity and non financial bonds are steadily declining,
- whereas holdings in bank accounts, life insurance, mutual funds and pension funds are on the rise and now represent the vast majority of their financial savings.

This trend is not good for savers as most bank savings accounts currently yield negative real returns (after inflation and fees), and as independent research show that real returns of long term and pension savings are on average disappointing, often negative and way below those of European capital markets[1].

It is not good as well for the real economy, growth and jobs, and - in particular – for SMEs. Lastly it is not good for corporate governance and for democracy as "agency owners" managing "other people's money" do not have their interest aligned to those of the beneficial owners, and typically have a shorter time horizon. In the 1960s, EU households directly owned about 40% of the EU listed companies; today only around 13%: we have moved from a "people's capitalism" model to a "financial capitalism" one where the deciders are financial firms, not the economic owners.

The CMU Action Plan released in September 2015 correctly identifies many issues, objectives and actions: "*Put simply, (CMU) is about strengthening the link between savings and growth. It will provide … better returns to investors*". It aims at "*boosting retail investments into capital markets and enhance individual confidence*", and requests the European Supervisory Authorities to work on the transparency of the performance and fees of long term and pension savings[2].

However, it currently lacks any action to reboot direct equity ownership by EU citizens and to revive equity culture – not only among households, but also among politicians and regulators who should lead by example and be proud of investing some of their savings into listed European SMEs. In addition, some other initiatives from the EU seem

[1] See in particular http://betterfinance.eu/fileadmin/user_upload/documents/Research_Reports/en/Pension_Report_2015_For_Web.pdf.

[2] http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A52015DC0468

to contradict the CMU efforts toward more transparency on savings returns: the recent proposed implementing rules for "PRIIPS " (retail investment products) eliminate all disclosure of past performance in the "Key Information Document" for savers, depriving them of even knowing if the product offered has ever made any money or not or has ever met its own investment objectives.

Also the CMU initiative assumes at least partly wrongly that EU households are extremely risk averse, and that this would mainly explain their reduced "appetite" for stock and bonds. Actually:

- EU households are less risk averse than institutional investors as they still have a much higher share of their financial wealth directly or indirectly in stocks than insurers for example;
- They cannot have any "apetite" for something that is no longer on their menu: for now several decades retail intermediaries have stopped talking about – and promoting stocks and bonds in favour of packaged and more fee-laden "packaged" products. Investment products being more "sold" than "bought", this is the actual main explanation for the decline in the direct ownership of securities by EU households.

Better Finance therefore advocates for:

- increased transparency on returns and fees of savings and investment products;
- more efforts put on the fight of market abuses, and of misleading information and advice (the CONSOB reports points to the desire from Italian individual investors to see the remuneration of investment intermediaries linked to their returns, which is not the case for now).
- A level playing field between packaged products on the one hand and stocks and bonds on the other hand at the retail point of sale; the exclusion of direct investments in such securities by EIOPA in its proposed "Pan-European Personal Pension" (PEPP) product is also inconsistent with the CMU initiative and goes against the interest of EU savers.
- Ensuring hat EU households can access low cost and diversified index funds in stocks and bonds (such as "ETFs"), as only 10 % of those are currently sold to individuals in Europe (versus 50% in the US); and also ensuring these products include ones that are based on broad market indices including mid and small caps, not only on a handful of less performing big caps as is currently the case in Europe (such as "Stoxx 50", "DAX 30", "CAC 40" or FTSE-MIB that includes only 40 different Italian large cap stocks).
- Revive equity culture at the retail point of sales as well as in schools and among politicians and regulators.

« *We need a simpler world … in which short chains of intermediaries provide more direct links between savers and the assets in which their funds are deployed…*
And we need asset managers whom we can trust to hold our savings for the long term and build knowledgeable, enduring relationships with the companies in which they invest. »

(Pr. John Kay, author of "Other People's Money", 2015)