Comments Template for Joint Consultation Paper concerning amendments to the PRIIPs KID (JC 2018 60)		Deadline 6 December 2018 23:55 CET
Name of Company:	Delta Capita	
Disclosure of comments:	Please indicate if your comments should be treated as confidential:	Public
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Reference	**Comment**	
General Comments		
Q1	The first point we'd highlight is that the inclusion of more prescribed information onto a KID could create severe issues in maintaining adherence to a 3 page limit. There may be some benefit to retail investors in prescribing the inclusion of past performance for *category 2* PRIIPs, as past performance may be useful in assessing products such as actively managed funds. Therefore including past performance on other category 2 PRIIPs would be beneficial for comparability. However, based on our experience working with a significant number of large PRIIPs manufacturers we see some strong disadvantages to including past performance results for PRIIPs	

	that fall under the other categories. The most significant issue with the existing PRIIPs regulation for a number of types of PRIIP is that the results of the existing performance scenarios are skewed by any strong historic drift. Including further information that includes or incorporates past performance will increase the impact of this issue. Including information on past performance that may give an unrealistic expectation of future performance cannot be mitigated just by including narratives that aim to minimise the investor's reliance on them. There is no certainty that a retail investor will give sufficient weight or attention to narrative that aims to limit their dependence on potentially misleading figures. In addition, including two different types of performance scenarios in the KID may be confusing to investors, as they may not understand the difference between the two sets of data or the implications of each on the product they are investing in.	
Q2	Yes - as noted in the paper, structured products are commonly offered to retail at or before the start of the structured products existence. There will be no meaningful past performance available.	
Q3	For many product types, we do not agree that it is appropriate for past performance to be included in any form.	
Q4	One major issue with simulated past performance is that it may create incentives to design a products that meets certain criteria to achieve a specific presentation when presenting past performance if investors relied on this to make investment decisions. Examples of this could be: 1. Where the product terms can be tweaked to result in a favourable backtest - For example: an underlying that falls 40%, but nevers drops more than 41% in the designated period could see a product created with a barrier at 58% instead of a more intuitive 60% to ensure the simulated past performance results do not show significant capital loss. , 2. A more complex example could involve an underlying index's rules being tailored in such a way that historic performance is presented favourably for no other reason than that is the desired result. We do not think the average retail investor will have the knowledge or financial sophistication to consider this – and in fact simulated past performance may falsely appear more reliable than simulated future performance to an untrained but sceptical investor as it appears less subjective.	

	Even without any element of intentional design bias to products or underlying terms to show favourable past performance, there is a risk that past performance could mislead investors. For most major equity indices there are often long periods of continual positive performance before a significant crash. A linked product offered near one of the peaks before the crashes could well show very misleading positive performance results and as stated earlier, trying to temper the impact of these figures with narrative is not a guarantee that the investor will give this due consideration.	
Q5	We maintain that for many product types, the inclusion of past performance (actual or simulated) is not desirable and could well do more harm than good to the investors understanding of the product. However if the decision is made to adopt this approach and mandate the inclusion of some form of historic performance, then where there is insufficient historic data we would suggest showing a similar underlying's history (and stating this is what has been used in the absence of sufficient performance history). Should this approach be adopted, then to ensure consistency guidance should be given to describe what manufacturers should do in the event products reference significant numbers of underlyings, where some have sufficient history and others do not – and situations where the real underlying is short by say 1 month from having sufficient history – should the proxy be used for the full required period, or should it just be used for the missing month?	
Q6	Although a slight improvement, we don't consider the amendments sufficient by a considerable margin. For category 3 products the prescribed methodology used to produce the performance scenarios is nearly always more complex than the product being offered to the retail investor. It will almost always be the case that the investor can not understand this methodology sufficiently to be able to put any misleading results into context, regardless of additional narrative that supplements the figures. Assuming there is no desire from the ESAs to revisit the performance scenario methodology at this stage we would make the following suggestions - The narrative should make it clear that the return an investor actually receives is likely to	

	be different from the scenarios shown - The results should not be referred to as estimates – they do not serve this purpose, especially given the overreliance on historic performance to generate them. - Some additional narrative could be included to highlight the fact that the prescribed methodology can result in displayed outcomes that are highly sensitive to the historic performance of the underlyings and could be significantly more positive or negative than the real spectrum of possible outcomes. - Consider renaming some of the scenarios away from language that suggests favourable and unfavourable outcomes. While we may understand that they are more favourable or unfavourable only in the sense that 90% of the other generated outcomes are lower/higher, if a retail investors sees a product where an “unfavourable scenario” generates a positive return, they’re much less likely to acknowledge any risk of capital loss or narrative below it that tries to explain that it might not be a reliable figure to base an investment decision on. We would however note that the adoption of the proposal to anchor the scenarios in the risk-free rate of return might limit the necessity for some of the above suggestions – and reiterate that making the scenario results more meaningful to the investor is preferable to narrative changes designed to mitigate potentially misleading results.	
Q7	We are generally supportive of the proposal to anchor any forward looking performance scenarios in the risk-free rate of return. This will have the benefit of removing the sensitivity to historic drift, but preserves the use of historic volatility. We are not supportive of the proposal to reduce the displayed number of performance scenario outcomes. We don’t feel the proposal to extend the historical period used really resolves any issues.	
Q8	For products where there is a reasonable basis for keeping drift from past performance in the performance scenario outcomes (e.g. actively managed funds where the fund manager’s track record is of relevance to an investor) this could be highlighted in the narrative and the investor referred to relevant material where this is presented.	

	We think this leads to a relatively easy choice between showing: a) More measured performance scenarios and narrative explaining why they may be too conservative in certain cases or b) The current situation where performance scenarios can be misleadingly positive (or negative) with narrative explaining why they shouldn't be relied on and the hope that investors give this narrative sufficient weight in their investment decision	
Q9	<u>Autocall feature proposal</u> A significant flaw in the proposed approach is that when combined with the reliance on historic performance to generate ther results, a 5 year autocall linked to an underlying with strong historic performance may well terminate in year 1 for both the favourable and moderate scenarios and in some even cases the unfavourable scenario. This means, of a potential 12 points of data across 4 scenarios and 3 holding periods, the investor will see just 4 unique points of data (3 points from the stress scenario, and then the same result across the other 3 scenarios in year 1). We do not think this allows for comparability of products given a similar product with no autocall feature (or the same product with a much higher autocall barrier) will show 300% more data points. While a consistent universal approach to autocall products hasn't emerged across the major manufacturers that issue autocall products to retail investors frequently, to our knowledge the vast majority of them have all adopted at least similar approaches that show figures at all holding periods, for all scenarios. We would strongly recommend considering approaches that maintain this status quo. A common and simple approach already widely used today is where the manufacturer propagates forward any autocalled paths up to the RHP and shows/uses the settled cash with no reinvestment. However at the moment manufacturers tend not to include any additional narrative to put the scenario results in the context of simulated autocall events (potentially from concerns that they will be deviating significantly from the prescribed text). Allowing additional narrative explaining the autocall feature in the context of the scenarios would	

	be more appropriate and beneficial to investors than the proposed methodology change set out in the Consultation Paper. Universal 3% growth assumption for the RiY calculation While this approach resolves some of the issues faced today, it introduces a new one that is potentially damaging to the retail market. For products that can never pay 3% or more per annum the impact of the costs shown under this proposal will always be higher than the real impact of the costs. This could present products with high levels of capital protection as having higher costs than they really do, as the trade-off for the capital protection typically results in a lower return. Given the KID is primarily intended to be used by retail investors, any change that introduces a bias away from capital protected products and towards more risky non-capital protected products should be treated with extreme caution. A similar solution that resolves all the same issues but avoids creating this new one could be to introduce a minimum universal growth assumption of 0% that kicks in if the moderate performance scenario performance is negative. (i.e add a minimum floor to the return used in the reduction in yield calculation of 100%) E.g. if the moderate scenario return is +10% , use 110% in the RIY calculation as you would today. If the moderate scenario return is -10%, use 100% in the RiY calculation. If the moderate scenario return is -80%, use 100% in the RiY calculation. We think this solution avoids punitively presenting capital protected products but also avoids risking that the investor doesn't appreciate the general impact of costs on the return due to moderate performance scenario results being negative.	
Q10	The display of cost figures does not appear to have been discussed in the consultation paper – currently UCITS presents raw costs while PRIIPs requires manufactures to show costs as a RiY.	

	Reduction in Yield is not an intuitive concept that retail investors always understand, particularly for product types that have a defined payoff where all the costs are implicit costs. There will need to be a harmonisation of approaches for UCITS structures to adopt the PRIIPs KID.	
Q11	It is unlikely that “PRIIP manufacturers can benefit from retail investors being better informed about the potential rewards from their products (e.g. potential reduced investor complaints)” through the “AMEND NARRATIVE EXPLANATIONS FOR PERFORMANCE SCENARIOS” without methodology change (i.e. if the figures are still confusing, the narrative isn’t going to limit investor/distributor queries or concerns). Aside from this we have no other comments.	
Q12	As highlighted in our responses to questions 1-5, for many products that qualify as PRIIPs, the inclusion of past performance information (simulated or otherwise) increases the risk that investors will rely on this information as a guide for future performance (rather than as a means for observing how the product behaves in a range of different market environments). Additional narrative that tries to mitigate this will be limited in it’s effectiveness. This is the most significant cost of the proposal to manufacturers, as it can’t be quantified, is potentially unlimited and can’t be capped or reduced through system efficiencies, internal control processes or higher upfront legal spend. The implementation costs of including simulated past performance (particularly for Category 3 PRIIPs) is likely to be almost as high as implementing the existing performance scenarios included in the PRIIPs KID today. However, many manufacturers already do something similar with respect to past performance as a part of their internal product governance decision making processes under MIFID II, so there’s potential for them to recycle these results provided the methodology is sufficiently aligned to any new proposal that is carried forward under the PRIIPs regulation.	
Q13	It is noted that the benefit and cost analysis was deliberately focussed on the performance scenarios. We feel that some of the other specific amendments referred to under question 9 carry considerable costs of a similar magnitude and should be considered to the same level of detail (particularly the autocall feature proposal and the 3% growth RIY proposal)	