
A Research Report by BETTER FINANCE
Better Finance, the European Federation of Investors and Financial Services Users, was founded in 2009 under the name of EuroInvestors. In 2012 it merged with 20 year old Euroshareholders.

Better Finance advocates for all financial services users: shareholders, bond holders, fund investors, pension plan participants, life insurance policy holders, bank savers, mortgage borrowers, etc.

Today Better Finance represents about 50 national associations which in turn have about 4.5 million European citizens as members. Its activities are supported by the European Union.

President: **Jella Benner-Heinacher** (DSW - Germany),
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Managing Director: **Guillaume Prache**
Why is this research report unique?

Long-term and pension savings appear to be one of the few retail services where neither the customers nor the public supervisors are properly informed about the real net performance for customers of the services rendered.

There is still no recent and comprehensive study on the real net pension savings returns for EU countries. Even OECD data is unfortunately quite incomplete.

The European financial supervisors still fail to report on the actual performance of products and services they regulate and supervise.

It is extremely and more and more difficult to find data on the returns of long term and pension savings.
OECD reports on pension fund real returns

OECD reports:
• cover 10 years maximum;
• 10 year reports do not cover France, Germany, Lithuania, Poland, Romania, Slovakia, Spain, Sweden and the UK;
• do not cover insurance regulated and bank regulated pension products (both occupational and personal);
• disclose «investment returns», not the returns net of all fees to the pension saver;
• before tax returns at saver level

Source: 10-year returns; Pension markets in Focus, 2017, OECD, p.16
Why are pension returns critical?

- The Pension time bomb: saving “more and for longer periods” as stressed by Public Authorities and the Industry is not sufficient, and even too often detrimental.
- **Unless long term net returns are significantly positive, saving early and significantly will not provide a decent replacement income through retirement**

<table>
<thead>
<tr>
<th>Annual net return</th>
<th>Replacement income</th>
</tr>
</thead>
<tbody>
<tr>
<td>negative 1%</td>
<td>10%</td>
</tr>
<tr>
<td>zero</td>
<td>12%</td>
</tr>
<tr>
<td>2%</td>
<td>17%</td>
</tr>
<tr>
<td>8%</td>
<td>49%</td>
</tr>
</tbody>
</table>

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Assumptions: no inflation, saving 10% of same activity income for 30 years (as recommended by Public Authorities), 25 year life expectancy at retirement, and excluding impact of taxes
EU Authorities do not report savings’ returns

Composition of EU households’ savings
(as used to assess retail investor returns)

The view of the EU Supervisor

<table>
<thead>
<tr>
<th>Shares</th>
<th>Interbank Money Market *</th>
<th>Bonds</th>
</tr>
</thead>
<tbody>
<tr>
<td>47%</td>
<td>42%</td>
<td>11%</td>
</tr>
</tbody>
</table>

Share of "packaged" products returns = 0%

Source: ESMA

The reality

| Deposits, 31% | Insurance & Pension funds, 25% | Equity, 22% | Mutual funds, 12% | Bonds, 7% |

Share of “packaged” products = 68%

Source: ESMA TRV nr. 2/2017

*Return proxy for bank deposits used by regulator is 1y Euribor: a (rather long) interbank money market rate, not a (shorter) retail banking rate.
1) Returns: Savings products have little in common with “capital markets” (index equity fund example)

Source: BETTER FINANCE research, fund manager
2) Returns: Savings products have little in common with capital markets (life insurance example)

Capital markets vs. Belgian individual pension insurance 2000-2017* performance

<table>
<thead>
<tr>
<th>Capital markets (benchmark index**) performance</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Nominal performance</td>
<td>127%</td>
</tr>
<tr>
<td>Real performance (before tax)</td>
<td>59%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Pension insurance performance (same benchmark)</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Nominal performance</td>
<td>56%</td>
</tr>
<tr>
<td>Real performance (before tax)</td>
<td>10%</td>
</tr>
</tbody>
</table>

*To end of 2017

** Benchmark is composed of 50% bonds (Barclays Pan-European Aggregate Bond Index) and 50% equity (FTSE All-World Total Index)

Sources: BETTER FINANCE, provider
3) Returns: Savings products have little in common with capital markets (Bulgarian Pension Funds)

Source: BETTER FINANCE
European Equity market performance: broad market vs. big caps market 18 years (2000-2017)

* Inflation used is HICP (2015 = 100), European Union 28. Annual average index
* MSCI Europe data used for 2000-2001 as proxy for STOXX All Europe Total Market (no data)
* Gross returns used for both STOXX All Europe Total Market and Euro STOXX 50 except for Euro STOXX 50 2000 (net returns)

We used the MSCI Europe GR index as a proxy for the 2000 and 2001 performances because we could not find those years for the STOXX All Europe Total Market index (these two indices are broad ones).

Source: BETTER FINANCE

Sources: Barclays Pan-European Total Returns & Eurostat HICP Europe 28 Annual Average Index
BETTER FINANCE methodology (1)

• **Coverage** – 16 Member States; 87% of the EU population. Three country profiles:
  - NL, DK, UK: pension funds assets represent far more than the annual GDP: real returns of private pensions is of crucial importance
  - ES, IT: Pensions mainly depend on the quality and sustainability of PAYG schemes
  - Countries in an intermediate position where the standard of life of retirees depends both on pension funds and PAYG schemes

• **Coverage** – Main product categories per Member State
  - A limitation of the report: the absence of residential property as an asset for retirement. But residential are often less suitable to retirement and dependency than financial assets
BETTER FINANCE methodology (2)

- **Time span** – 18 years (Dec 1999 - Dec 2017) *whenever available* (which is too often not the case). Includes:
  - Two market upturns (2003-2006; 2009-2016)
  - Two downturns (2001-2003; 2008)

- **Net Real return**
  - Nominal returns (net of fees and commissions borne by pension savers, including entry and exit fees whenever possible)
  - minus inflation (HICP)
  - minus taxes (data permitting: not often)

- **Compounded and geometric annual mean returns** for investing at end of 1999 (actual long-term performances, 18 years)
Most pension products’ returns recently improved but still very far from capital market returns

**Real geometric average annual net returns of Pension Savings (%)**

<table>
<thead>
<tr>
<th>Pension Product</th>
<th>Return (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>The Netherlands Occupational Pension Funds, 2000 - 2017</td>
<td>2.65%</td>
</tr>
<tr>
<td>Germany Pension Insurances 2000-2017</td>
<td>2.85%</td>
</tr>
<tr>
<td>France Life Insurance, Capital guaranteed, 2000-2017</td>
<td>1.90%</td>
</tr>
<tr>
<td>Belgium Occupational Pension Plans (IORP), 2000-2017</td>
<td>1.90%</td>
</tr>
<tr>
<td>Belgium Pension Savings Funds, 2000-2017</td>
<td>1.89%</td>
</tr>
<tr>
<td>Bulgaria* Professional pension funds 2001-2017</td>
<td>1.67%</td>
</tr>
<tr>
<td>Italy Closed Pension Funds, 2000-2017</td>
<td>1.41%</td>
</tr>
<tr>
<td>France Corporate savings plans, 2000-2017</td>
<td>0.81%</td>
</tr>
<tr>
<td>Italy Open Pension Funds, 2000-2017</td>
<td>0.10%</td>
</tr>
<tr>
<td>Spain Pension funds (weighted average), 2000-2017</td>
<td>0.05%</td>
</tr>
<tr>
<td>The Netherlands Life Insurance, 2000 - 2017</td>
<td>-0.11%</td>
</tr>
<tr>
<td>France Life Insurance, Unit-linked, 2000-2017</td>
<td>-0.82%</td>
</tr>
</tbody>
</table>

*50% Equity (Stoxx All Europe Total Market) - 50% Bonds (Barclays Pan-European Aggregate) yearly re-balanced

**Source:** BETTER FINANCE research
Why too often low returns for pension savers?

Return attribution (1)

1. Fees and commissions
   ✓ Introduction of transparent, limited and comparable charges in the UK, less advanced in other countries

2. Asset mix
   ✓ Striking differences across countries in pension funds’ asset allocation
   ✓ Overall, the dominant asset class is fixed income (bills and bonds), not equities
Why low returns for pension savers?

Return attribution (2)

3. Capital Markets’ Performances (see previous slides)
- The only country with a negative average return on the equity market on the whole period (2000-2017) was Italy (-1.65% annually);
- Over the last 18 years, European bonds enjoyed a very positive nominal return due to capital gains (+130%).

4. Asset manager competence
- The majority of funds underperform their relative benchmark;

5. Taxation
- EET regime is predominant: contribution and investment returns are exempt; benefits are taxed;
- Part of pension benefits can be withdrawn as a tax exempt-lump sum in some cases;
- “Financial repression” in several countries.

6. Inflation
- Inflation rates had a severe impact on real returns in several countries (EU28 average: 1.8% annually).
The future outlook

- Fees and commissions are not going significantly down and are still very opaque
- Asset allocation has tilted towards more fixed income and less equity in the recent years
- Financial repression (“non conventional” monetary policy coupled with forced LT savings into Sovereign bonds) is unabated in Europe
- The interest rates decades long decline is over: it has provided exceptionally high fixed income returns over the last decades
- Taxes on long term savings are still on the rise
  - EU reforms:
  - PRIIPs Key Information Document
  - transparency on performance (CMU Action recently started)
  - PEPP
“Sunlight is said to be the best of disinfectants; electric light the most efficient policeman.”

(Louis D. Brandeis, Other People’s Money and How the Bankers Use It, 1914)

Transparency is very poor and deteriorating for actual net returns of long term and pension savings

1. **Restore and standardize relative past performance disclosure for all long-term and retirement savings products:**
   - Re-instate standardised disclosure of past performance compared to objective market benchmarks on a period consistent with the type of product (long-term savings);
   - Eliminate future performance scenarios or at the very least make the PRIIPs’ KID compliant with MIFID II rules on performance disclosure;
   - Extend the UCITS exemption from the PRIIPs Regulation by a minimum of three years;
   - Impose and enforce better disclosure of total fees and commissions (direct/indirect), funding status, transfer/exit possibilities and conditions;
   - Extend the PRIIPs’ KID principle (concise, standardized, and plain language document) to ALL long-term and pension savings products

2. **Address important omissions in the scope of the EC’s 2017 request for “the European Supervisory Authorities (ESAs) to issue recurrent reports on the cost and past performance of the main categories of retail investment, insurance and pension products”**.

3. The co-legislators entered (September 2018) the crucial triilogue phase of the negotiations should make sure to, at least, protect the long-term purchasing power of the life-time savings of EU citizens in the default investment option.

4. **Simplify, standardise and streamline the range of product offerings.**
5. Better align the pricing of investment products with the interests of savers and end biased advice at the point of sale and guarantee competent advice on long-term investments.

6. Improve the governance of collective schemes.

7. Establish EU-wide transparent, competitive and standardised retail annuities markets.

8. Grant special treatment by prudential regulations to all long-term & pension liabilities allowing for an adequate asset allocation.


10. EC to follow up on their “Consumer Financial Services Action Plan” released in 2017 and go beyond the non-binding “Key Principles for Comparison Tools”.

11. Improve financial literacy: Introduce financial mathematics’ basics as part of school curricula and allow at least a part of their financial education efforts to be guided by independent bodies.
The full version of the Report is available for download at www.betterfinance.eu

Thank you for your attention!