BETTER FINANCE

The European Federation of Investors and Financial Services Users
Fédération Européenne des Épargnants et Usagers des Services Financiers

Will you afford to retire?

The Real Return of Long-term and Pension Savings

Sébastien COMMAIN, Senior Research & Policy Officer, BETTER FINANCE

Brussels, 30 Nov. 2023

“Will you afford to retire?”

A RESEARCH PROJECT TO SERVE RETAIL INVESTORS’ INTERESTS

"The Real Return": A long story, continuing

A long history…

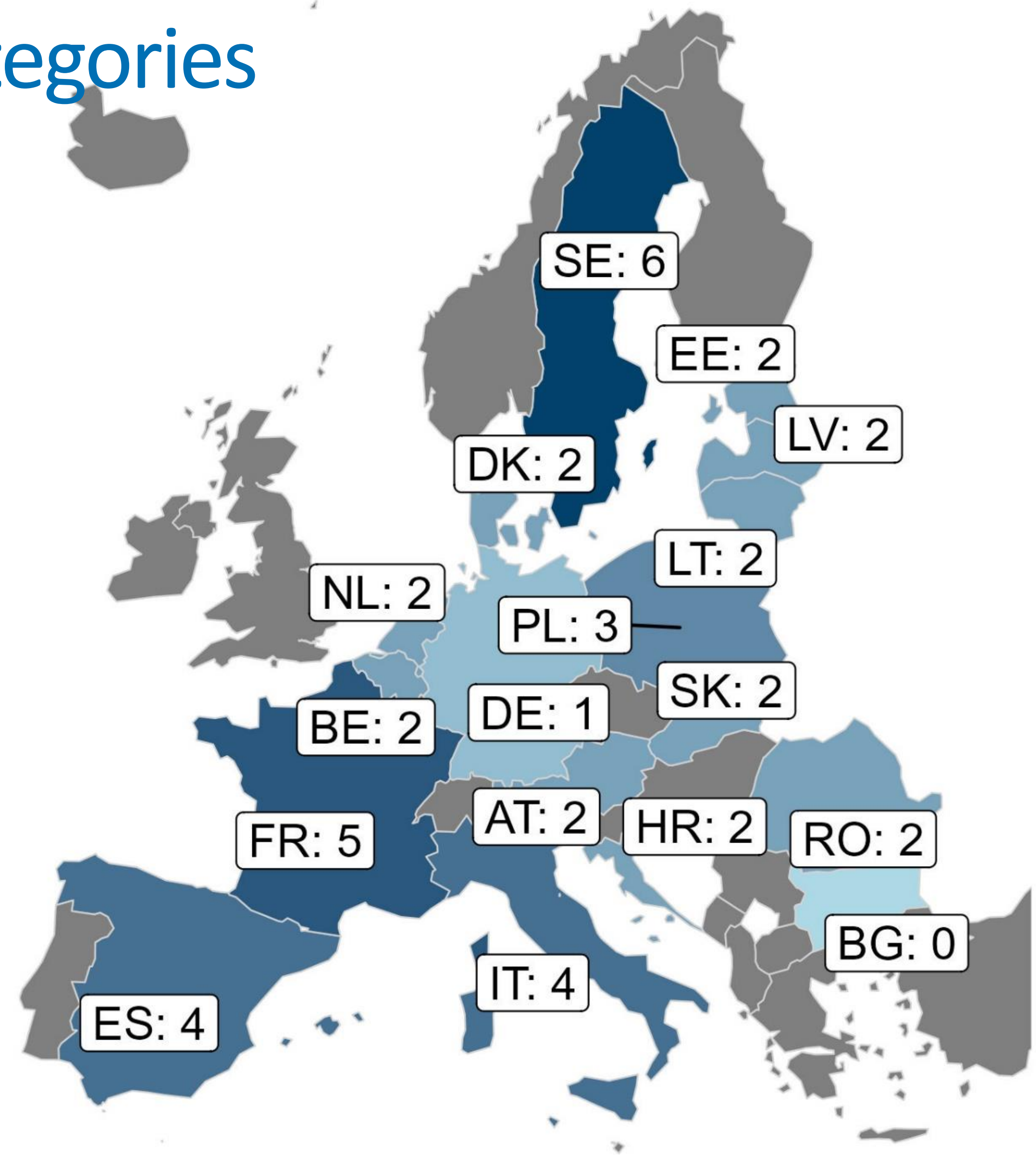
- 11th edition:
  - From 3 to 17 (well, 16) countries
  - Consolidating the legacy
  - Opening a new chapter
- New title, same ambition:
  - "Will you afford to retire?", a question for all ages
  - Raise awareness about long-term financial planning
  - Highlight the cumulated effects of costs and inflation on long-term savings

Still unique

- All providers in a product category (pension funds, IBIPs), not a sample
- Distinguishing between pillars
- Up to 23 years of data on:
  - returns (gross, net, real net)
  - costs & charges
  - asset allocation
- Description of and information on pension systems

16 countries, 43 product categories

- Real net returns calculated for 43 product categories
  - 21 Pillar II
  - 22 Pillar III products
  - Performance data for 3 to 23 years.



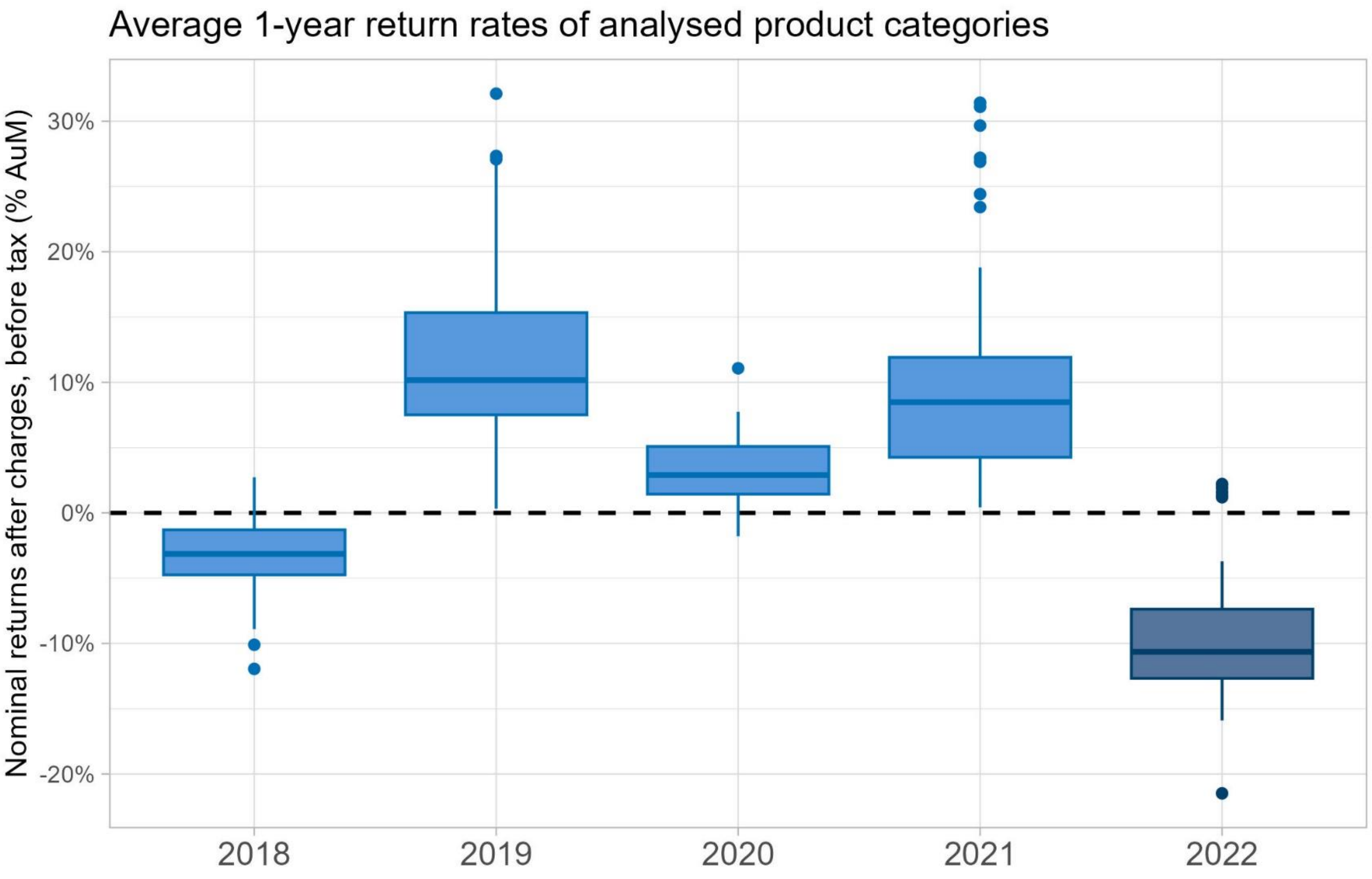
2022, a catastrophic year for investors

Average nominal returns positive for only 6 out of 41 products

Best performing product category: +2.2%

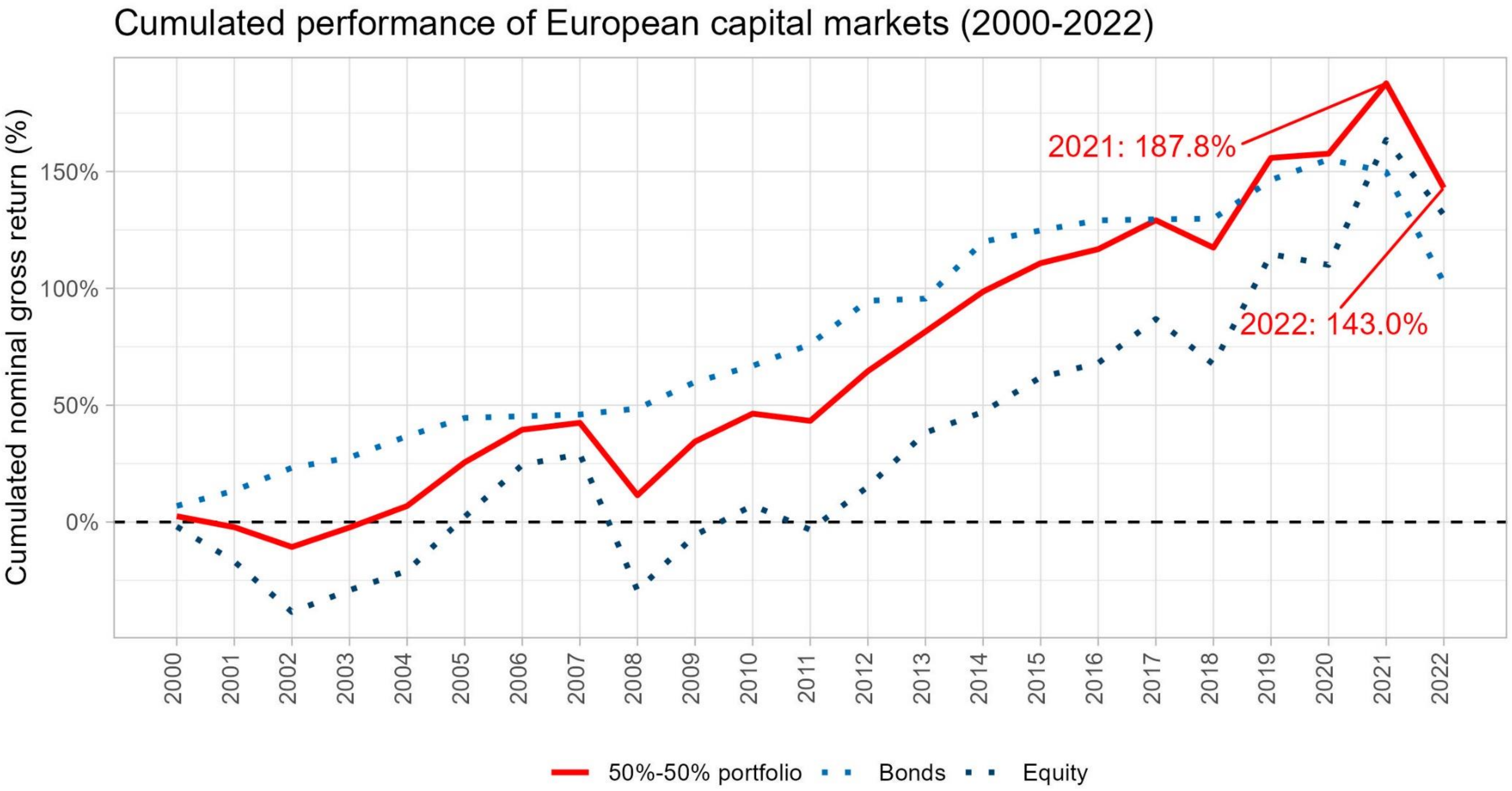
Worst performing product category: -21.5%

Average performance: -9.2% (vs. 10.8% in 2021)



BETTER FINANCE calculations.

Capital markets plunged…

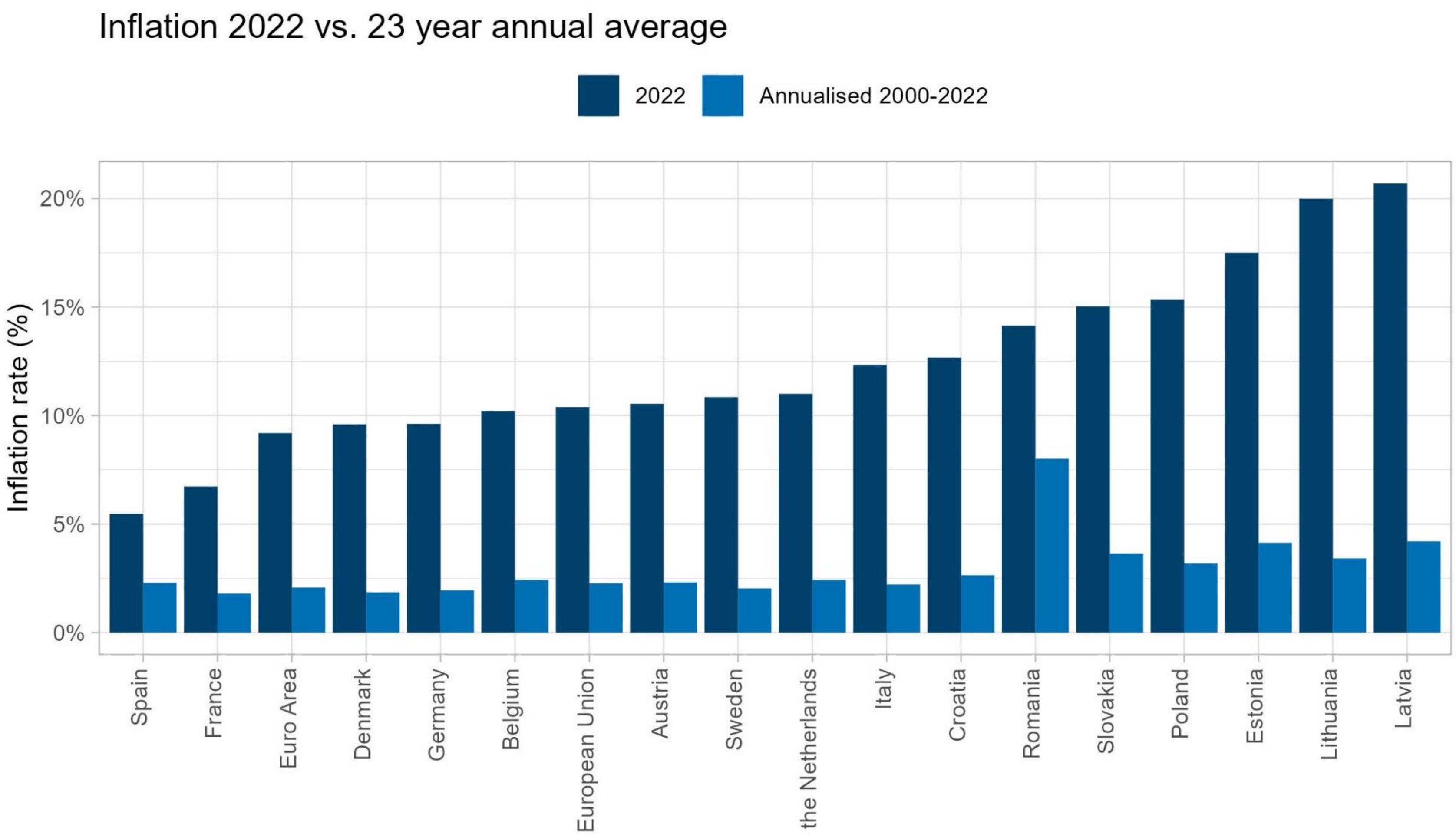


Equity index: STOXX All Europe Total Market (gross return);
Bonds index: Barclays Pan-European Aggregate Index (gross return);
The 50%-50% portfolio is rebalanced annually.

… and inflation peaked…

All countries affected, but to varying extents:

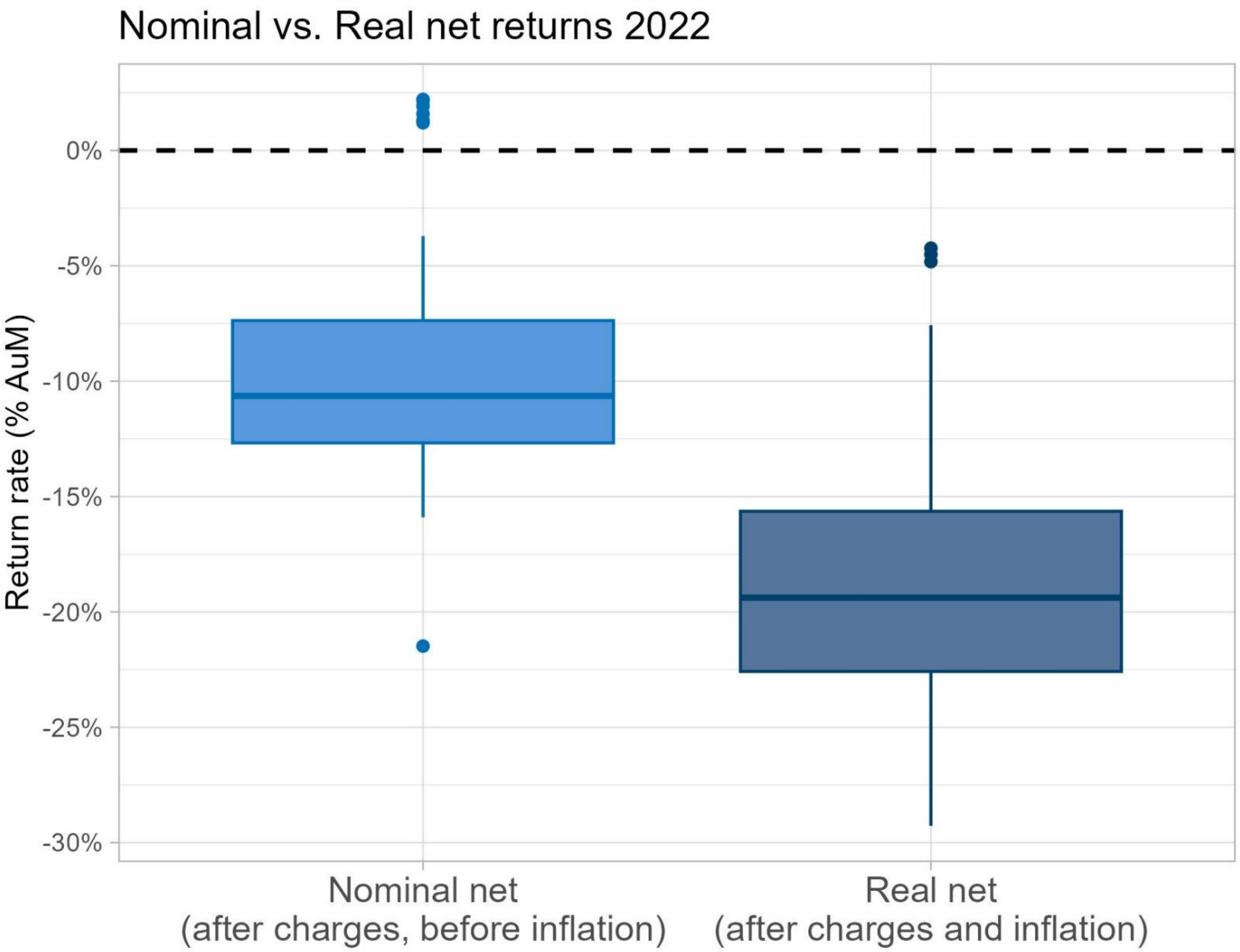
- EU average: +10.4%
- Spain: +5.5%
- Latvia +20.7%



Eurostat data (HICP monthly index); BETTER FINANCE calculations.

… leading to major losses in real terms

- Rising inflation further compounds the poor performance of capital markets in 2022.
- In real terms, return is negative across all products in our sample.



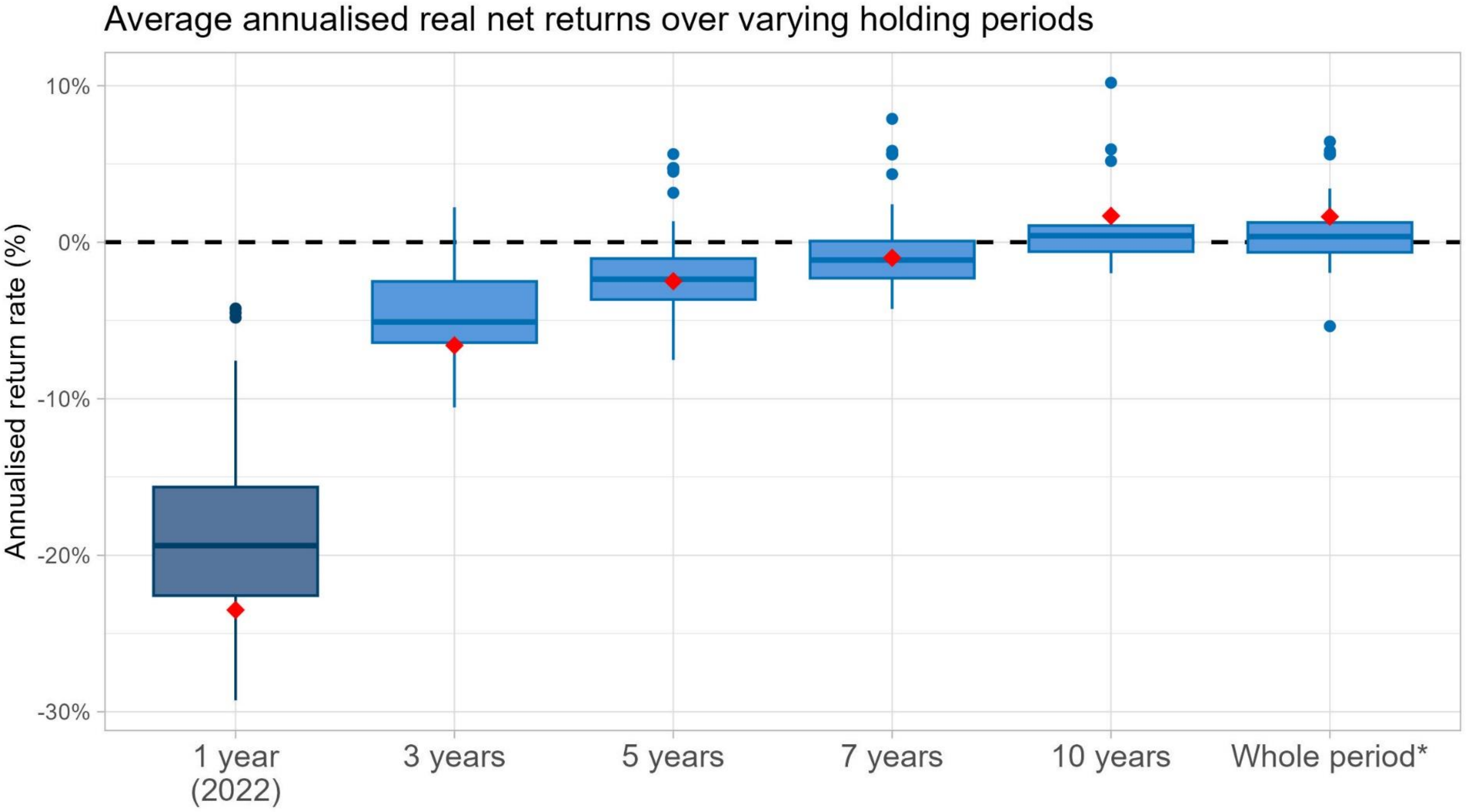
BETTER FINANCE calculations.

Good years, bad years…

A LONG-TERM PERSPECTIVE ON LONG-TERM SAVINGS

Long-term perspective: Still inadequate…

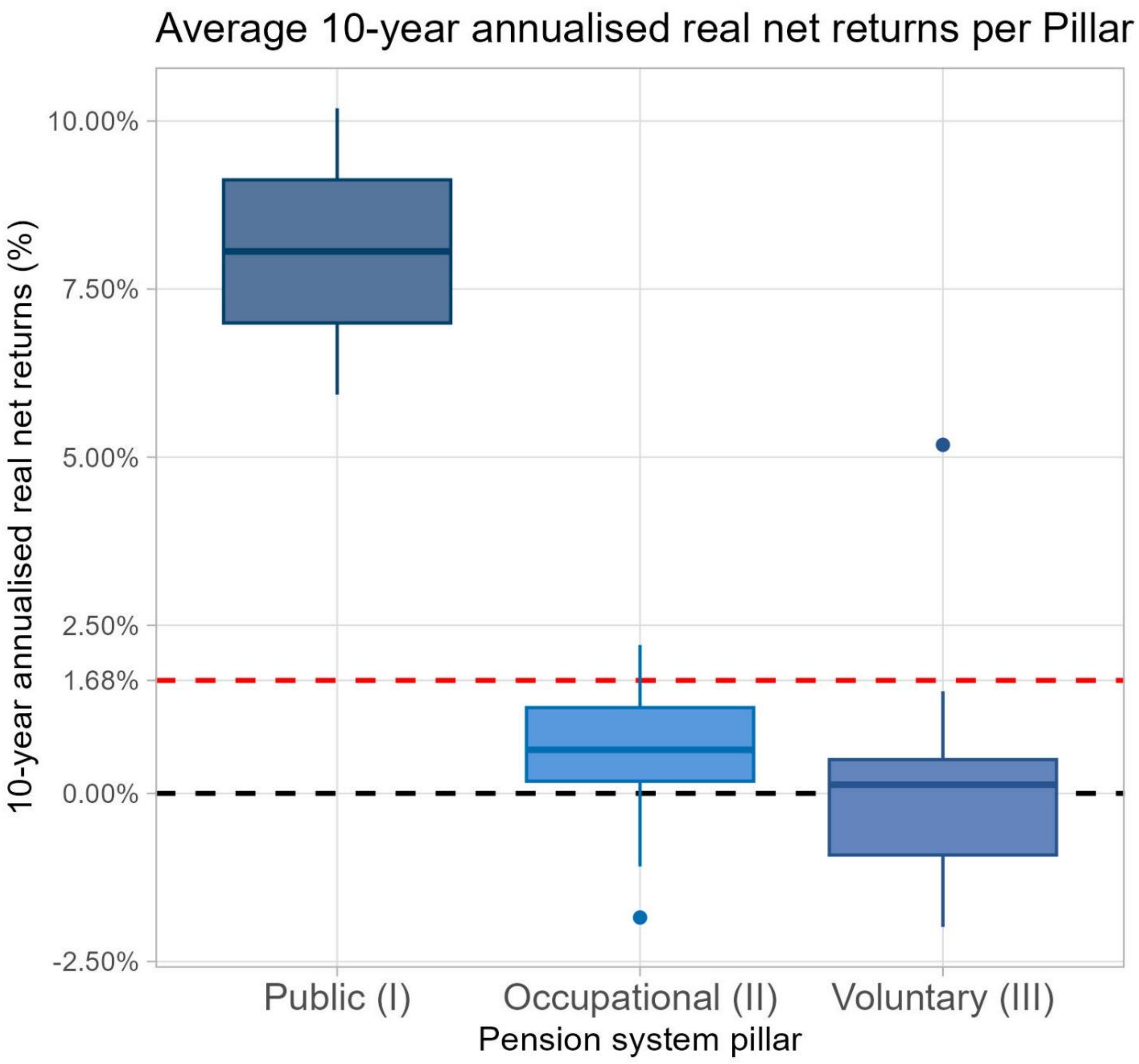
- Negative real net returns for 16 out of 43 product categories on their maximum reporting period (3 to 23 years
- 10 years: negative for 12 out of 40.
- Only 12 out of 43 beat their capital market benchmark



BF calculations;
* The reporting period varies across products (earliest year: 2000)

Who performs best?

- Best performing over 10 years: **Sweden's AP7 Såfa (Pillar I, +10.2%)**
- **Occupational (Pillar II) schemes *generally* perform better** than voluntary (Pillar III) savings products (lower costs)



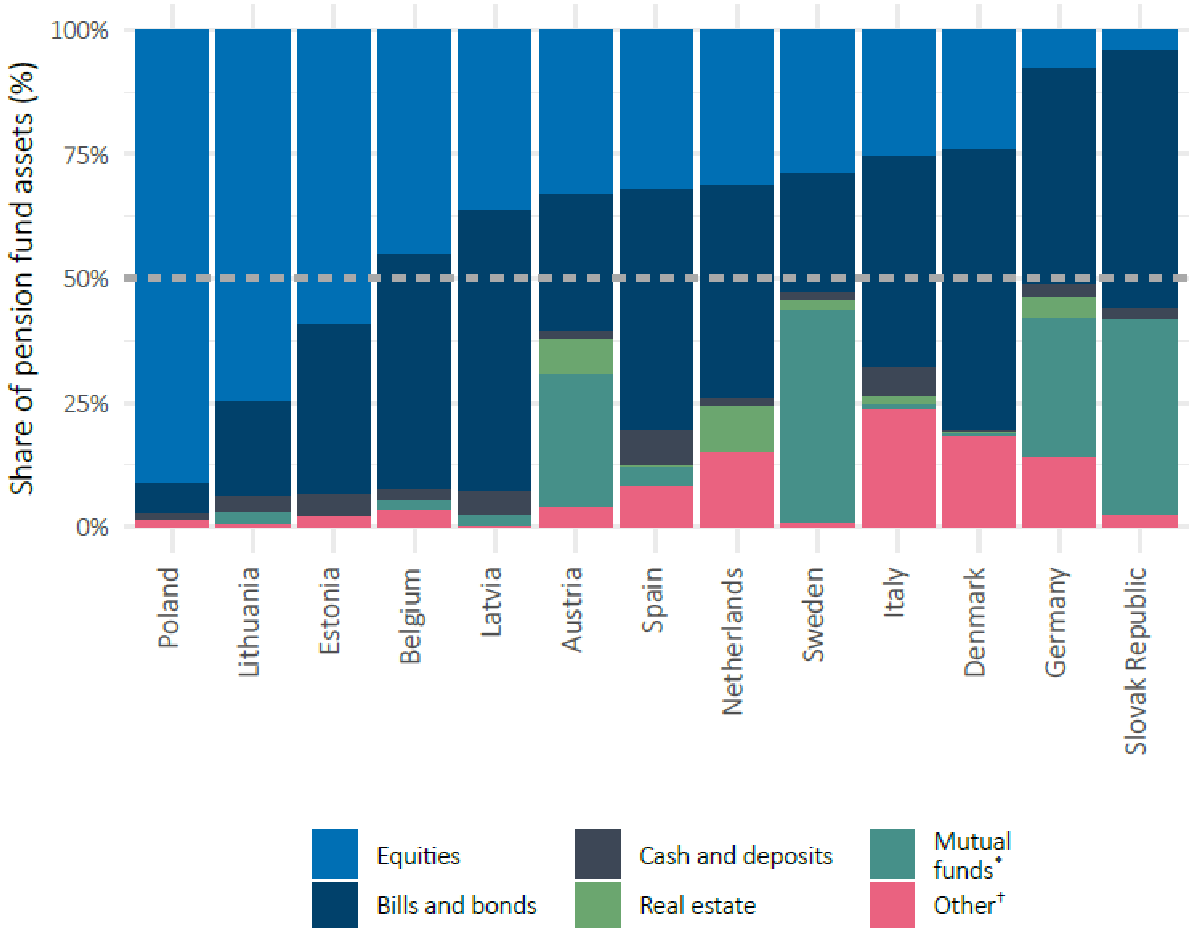
BF calculations;
Returns after charges and inflation.

PERFORMANCE DRIVERS

Asset allocation: Too conservative?

- Fixed-income assets dominate investment of most of the analysed products
- Low volatility at expense of long-term returns?

Figure GR.12 – Average asset allocation of pension funds per country (% of total assets)

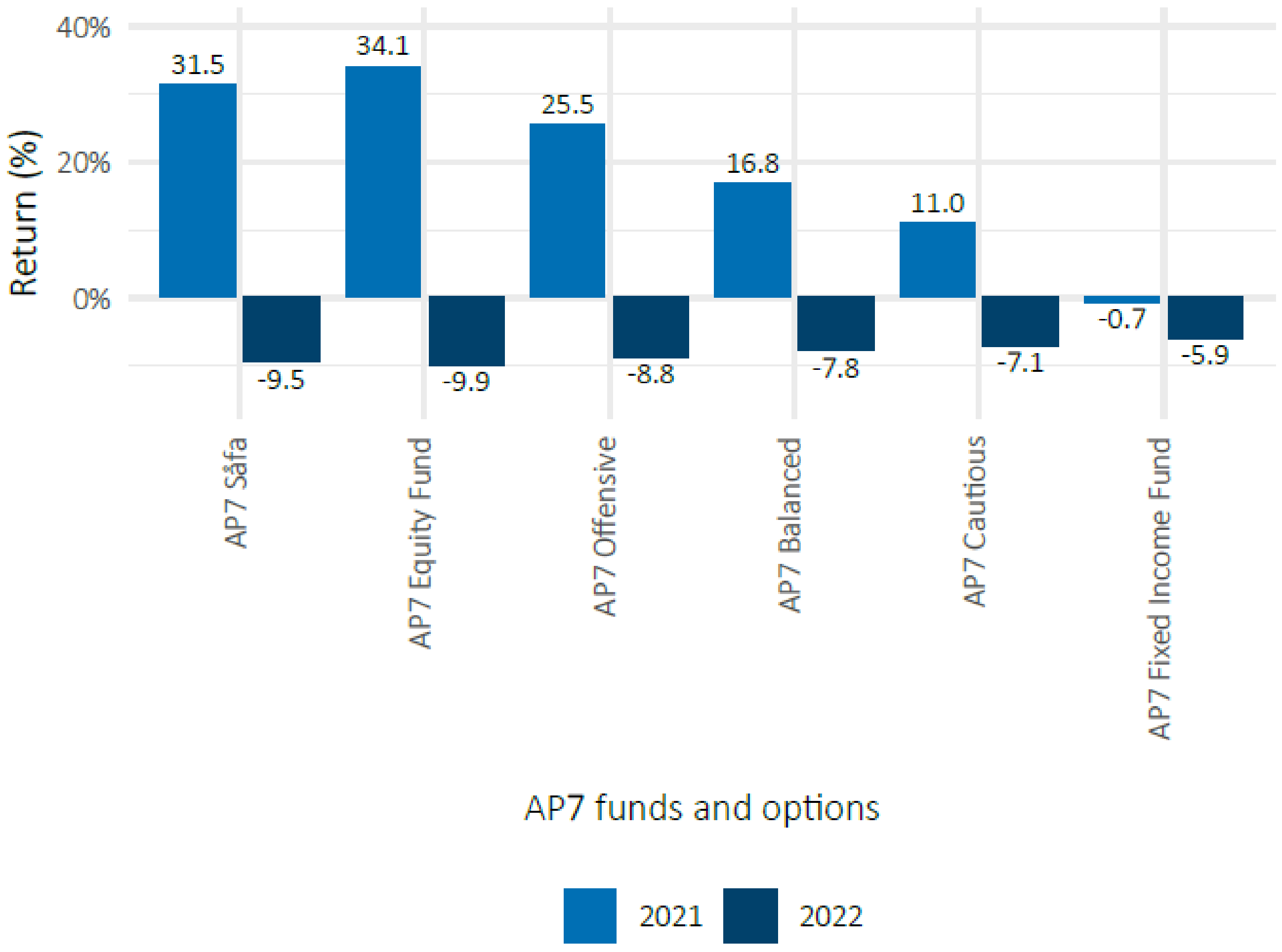


Data: OECD, *Funded Pensions Indicators*, 2023; * Where data are available, a look-through approach is applied and amounts invested in mutual funds are re-assigned to the category of the underlying assets; † Includes loans, unallocated insurance contracts, hedge funds, private equity funds, structured and other products.

Asset allocation: Too conservative?

- Best performing product: Sweden's AP7 Såfa
  - Life-cycle approach
  - 100% equity until age 55
  - Still 33% equity after retirement

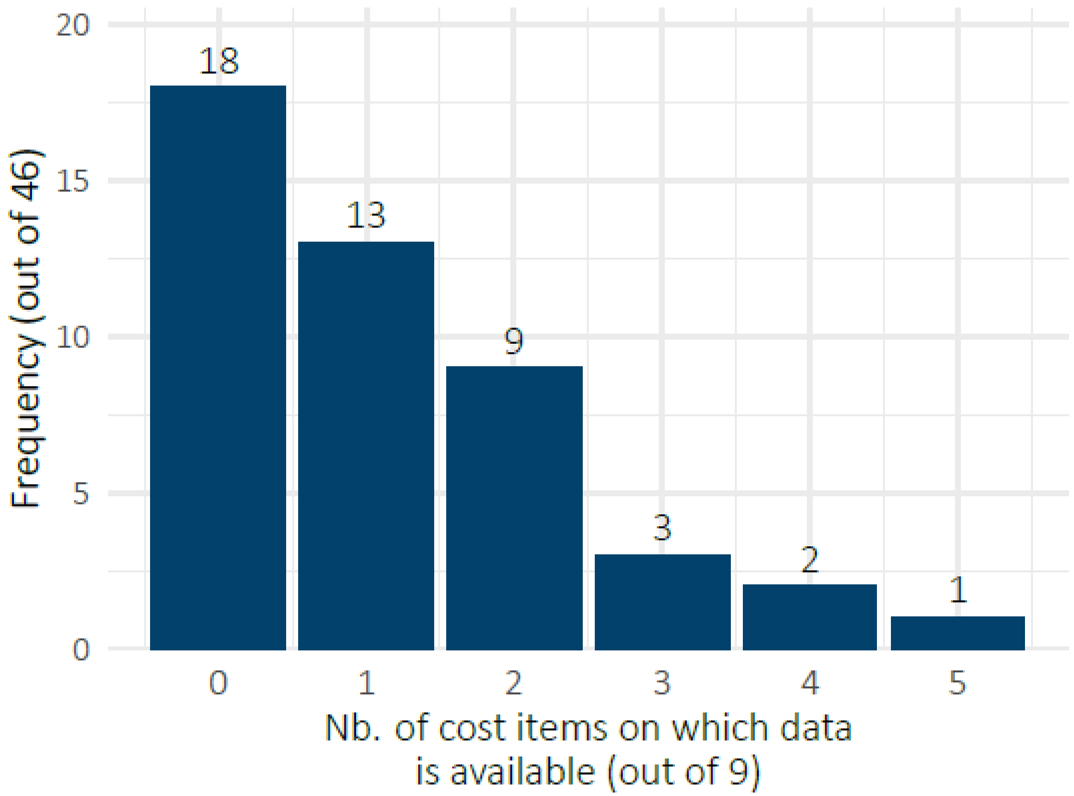
Figure GR.10 – Returns of AP7 funds and investment options 2021-2022



Data: AP7, Annual and Sustainability Report 2021, 2022

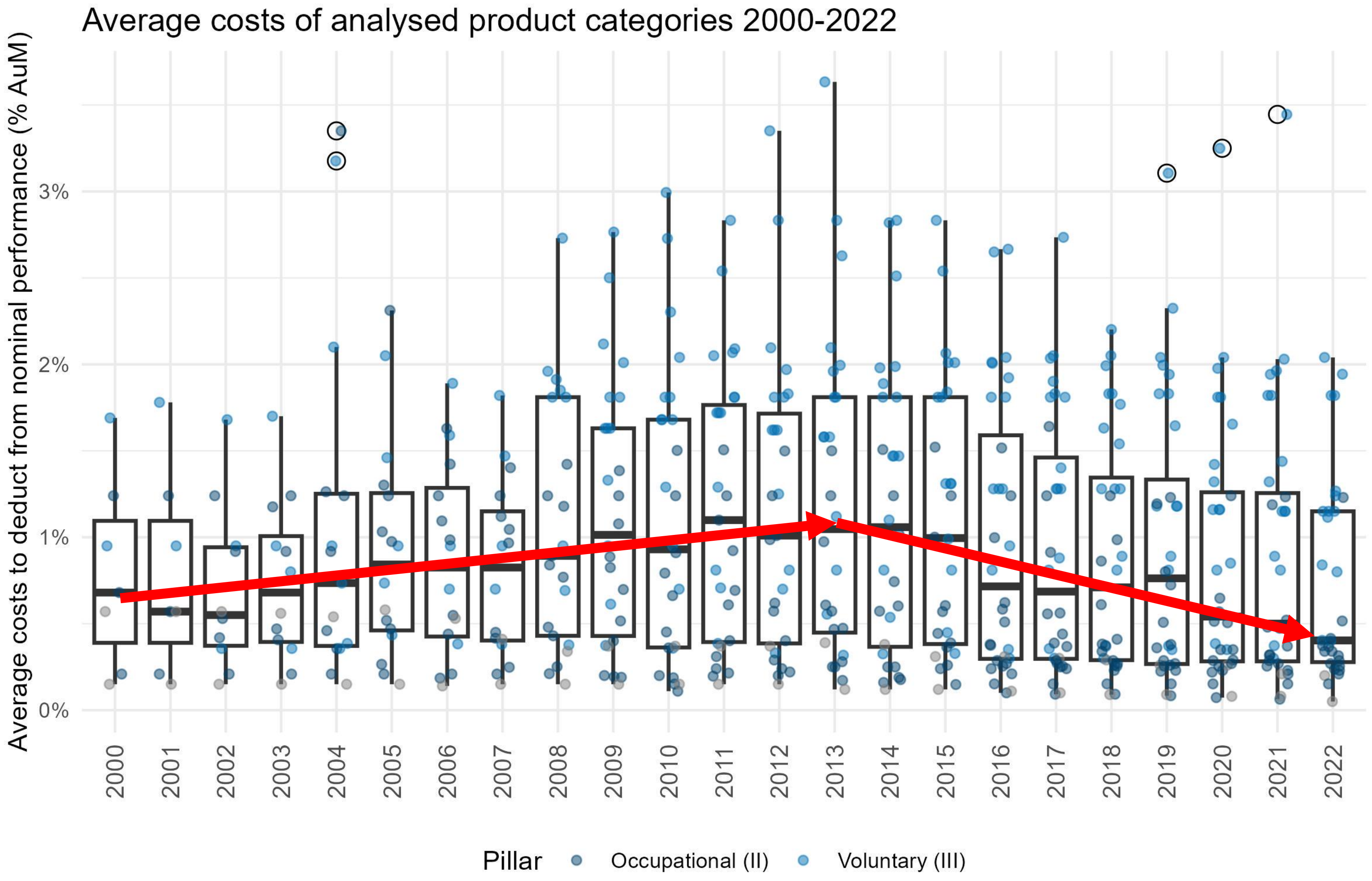
Data on costs: Scarce and hardly comparable

Figure GR.14 – Availability of cost & charges data for 2022



- Data on costs and charges still difficult to obtain in many cases
- Great variation across and within countries
- For only 28 of the 46 product categories in our sample do we have at least one cost item in 2022

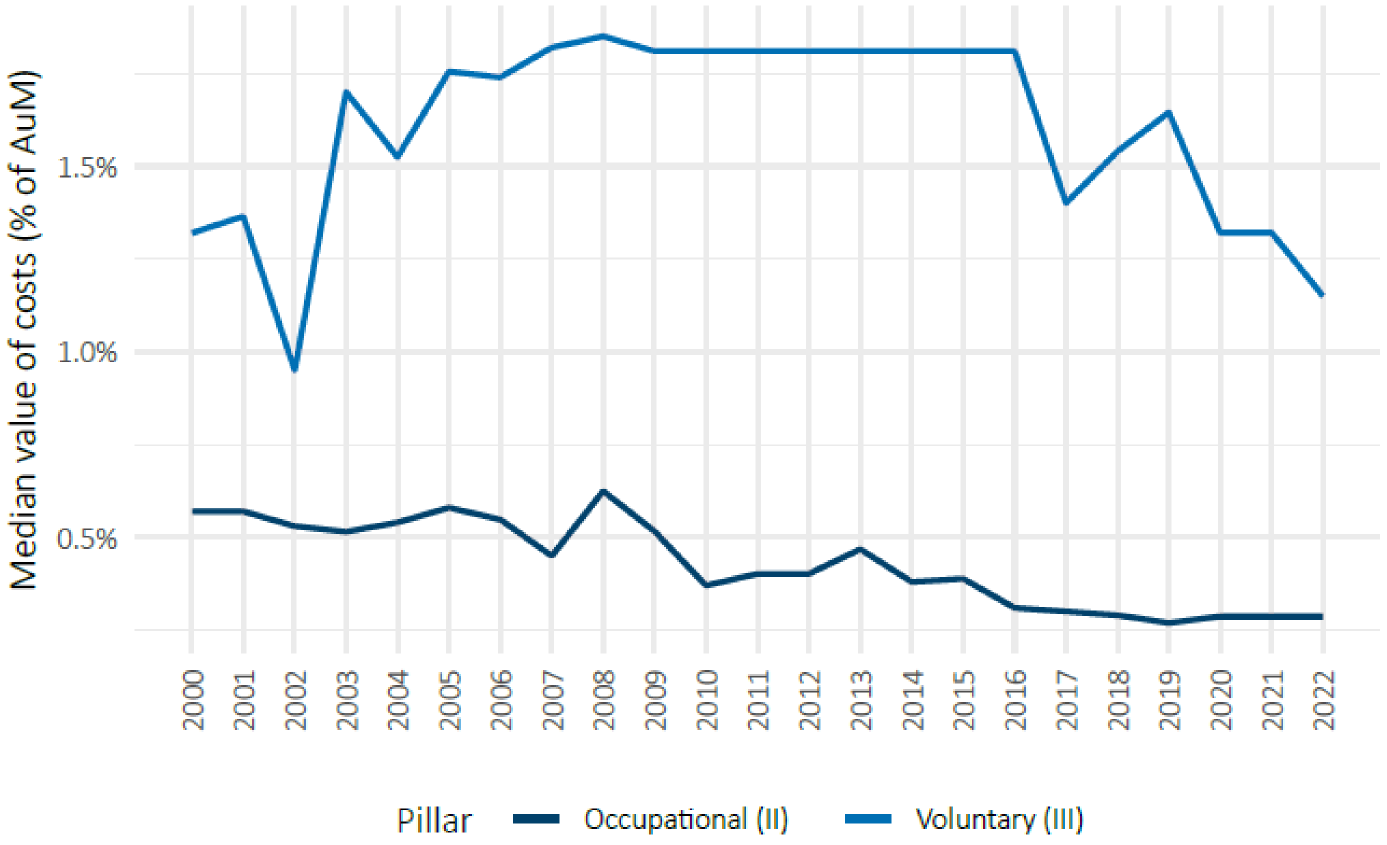
Level of costs: Some good news?



Data: Multiple sources (see Country Cases); Calculations: BETTER FINANCE; Outliers with costs above 4% are not displayed.

Pillar III: Structurally higher costs?

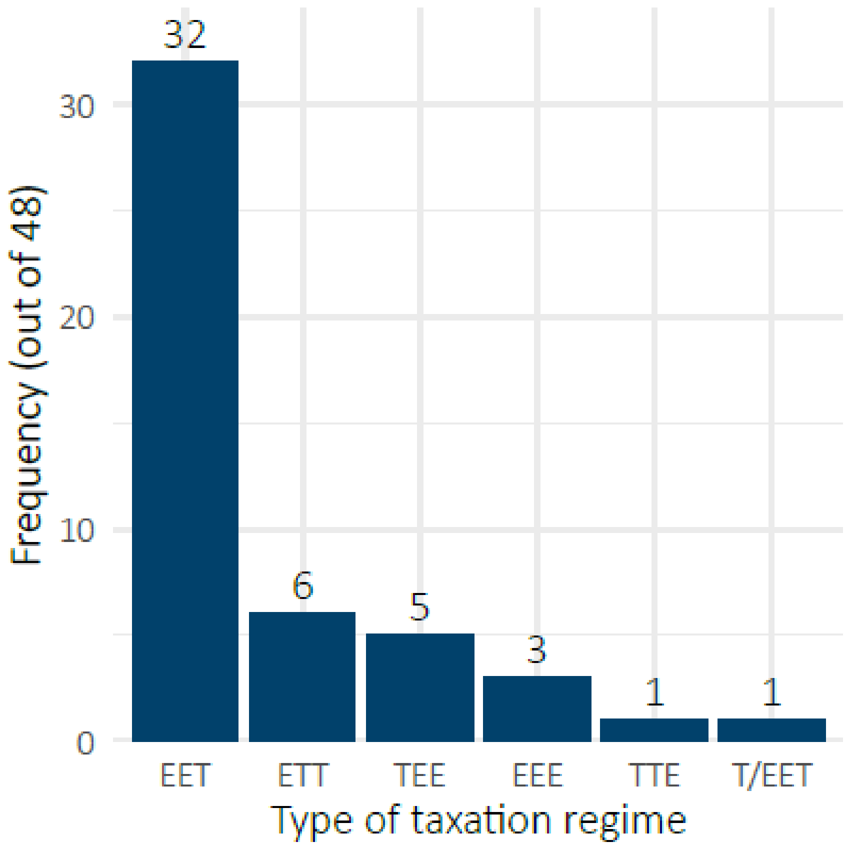
Figure GR.16 – Median value of the average costs of analysed product categories per pillar 2000–2022



Taxation

- Dominant “deferred taxation” regime
- But tax calculated on nominal pension amounts…
- … which are depreciated by inflation

Figure GR.19 – Distribution of product categories per types of tax regime



Conclusions

- Most of the products analysed do not generate sufficient real net returns to significantly improve savers' retirement income.
  - Costs are often eating away a significant part of the returns
  - Investment policies generate insufficient nominal gross returns to compensate for both costs *and* inflation
- Overall, level of costs decreasing, but still many very expensive products
  - Pillar III products structurally more expensive than Pillar II: a question of distribution?
  - Transparency, accountability and benchmarking: Justify and quantify the costs of products

Thank you for your attention

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"Will you afford to retire? How to ensure better pension adequacy"

Better Finance Pensions Roundtable

Presenters: Valerie Mariatte-Wood
Date: 30 November 2023

European Insurance and
Occupational Pensions Authority

Pension gaps and consumers' confidence in their retirement

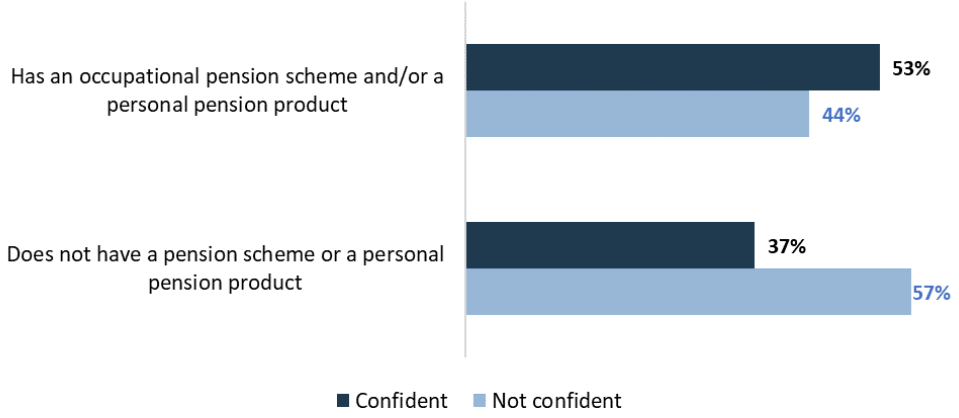
EU consumer financial confidence in their retirement is worsening – this can be partially due to inflation

- **Moderate/low penetration of pension services** across the EU
- Only 23% of EU Consumers reported being members of an occupational pension scheme and 19% of owning personal pension product*

- The percentage of European consumers that are financially confident in their retirement has **decreased by 3 percentage points** from June 2022 to July 2023
- Clear gender gap in financial confidence in retirement due to the persistent gender pension gap (47% vs 37%)

- Consumers that are part of an occupational pension scheme or have a personal pension product **feel more financially confident in their retirement** (53%) than those without an occupational pension scheme or personal pension product (37%)

EU consumers' financial confidence in their retirement (EIOPA's Eurobarometer)



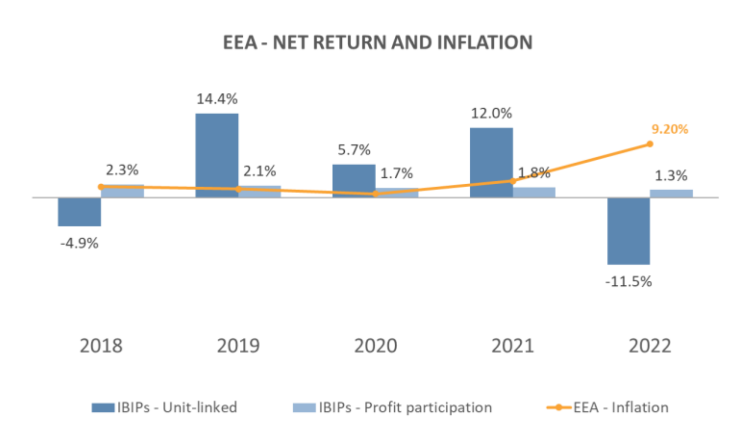
*These figures come from a representative sample of EU consumers with various occupational status such as self-employed (7%), employee (38%), manual worker (6%), retired (28%), others not working (19%) and should be interpreted within that context.

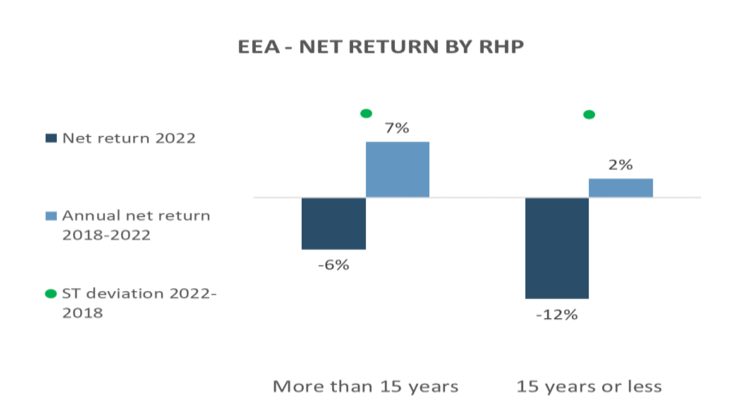
Insurance-based investment products (IBIPs) costs and returns

Costs of IBIPs remain high and underlined the need for long-term perspective to measure value

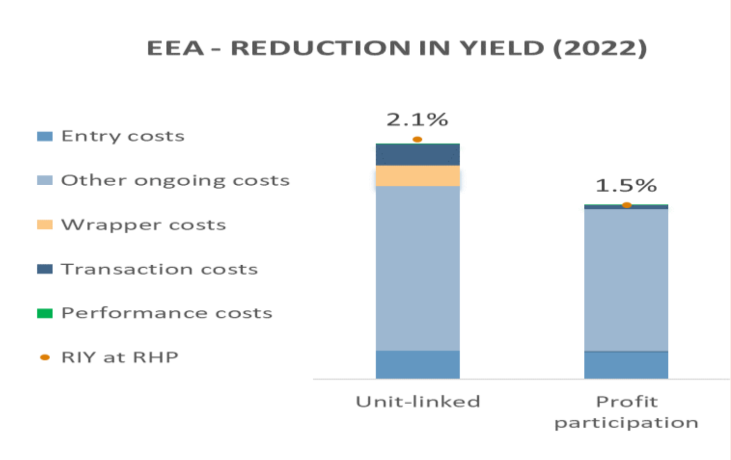
NET RETURN

- IBIPs offered positive returns over the period 2018-2022, despite the significant drop in 2022
- In real terms, in 2022 all IBIPs on average reported negative returns
- While the trends presented are averages across the EU, substantial differences exist. In particular for UL products performance. The Recommended Holding Period (RHP) has a clear impact on returns





COSTS



- Costs remain high and UL products have higher costs than PP products
- RHP does not seem to impact costs
- Dispersion of costs is higher for UL products than PP ones

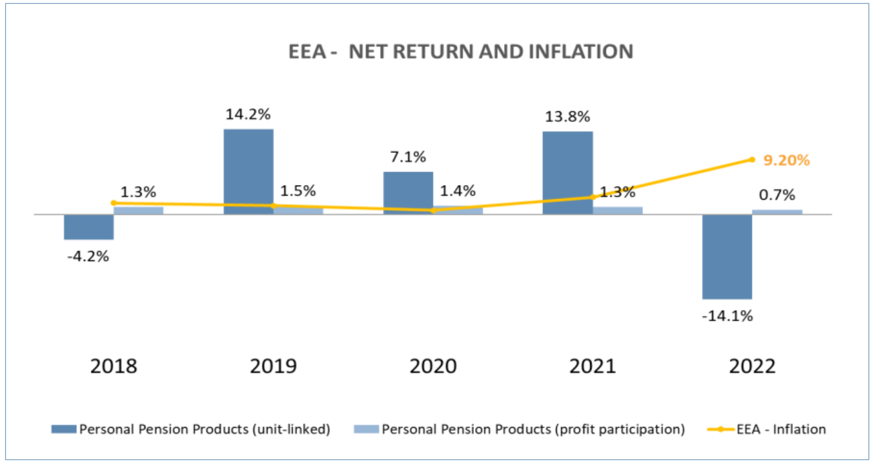
Personal Pension Products (PPP) costs and returns

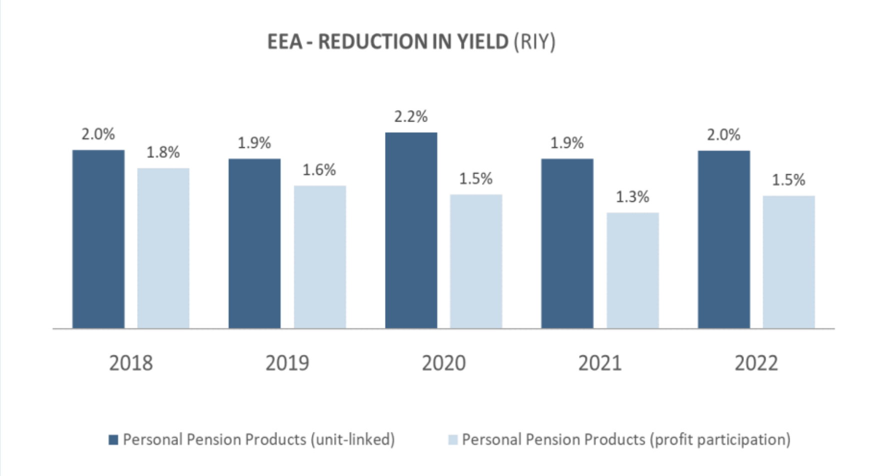
No been significant changes in PPPs costs and returns - on average slightly higher returns than IBIPs

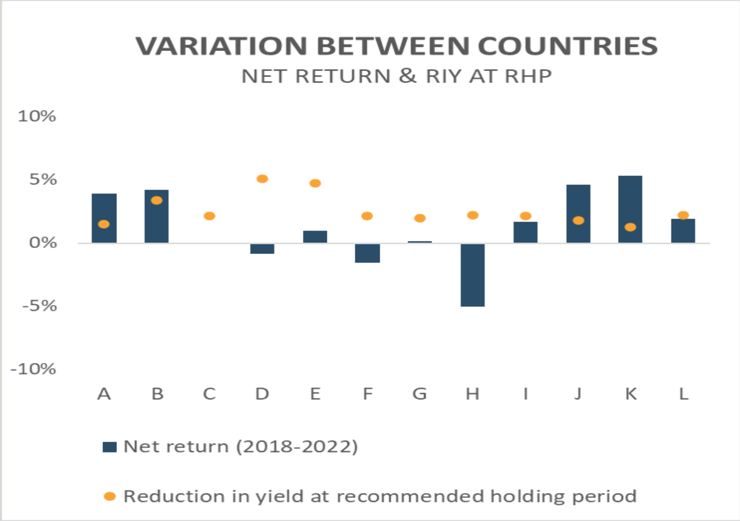
- In 2022, the performance of PPP followed the same trend that IBIPs, however, PPP unit-linked had offered higher net return during previous market upturns

- High volatility observed on PPP UL poses concerns if there are not life cycling strategies in place

- PPP costs have remained stable in the past years. However, decreasing costs of PPP observed since 2018 are receding







- PPP in EEA are heterogenous making the comparison difficult

- In some Member States, PPP_UL shows a balanced relationship between costs and net returns, whereas high costs and low return also coexist in other markets

EIOPA’s work – closing the gap

Tracking systems and increased transparency to close the gap and dashboard to assess adequacy

Overview	▪ More clarity on one’s pension situation fosters pension knowledge and empowers individuals to make informed decisions about savings, investments, and pension plans. Also, in light of the shift from DB to DC ▪ Old-age dependency ratio (65+/20-64) in the EU is projected to rise from 34.4% in 2019 to 59.2% in 2070 – gaps can increase
EIOPA’s work	▪ EIOPA’s advice on pension tracking systems focused on identifying best practices, allowing flexibility to Member States in terms of choosing functionalities, costs and forms of governance – this so Members can give consumers tools to check accrued entitlements and projected retirement income in one place, in a simple and meaningful manner ▪ The advice covers front-end aspects (using behaviourally informed solutions) and back-end aspects in terms of consistency of data and comparability. It also covers governance aspects ▪ EIOPA’s advice on dashboard aims at identifying data gaps for projections and developing methodologies for dashboards ▪ Dashboards should easily communicate pensions situation, be comprehensive, comparable and up to date ▪ EIOPA is also putting a greater emphasis on DE&I work to close gaps
What NCAs report	▪ NCAs reported that consumers in countries with PTS valued the clear and succinct pension-related information received via their PTS ▪ Considering improvements in pension disclosure and transparency as well as thanks to financial literacy programs and pension tracking systems, 50% of responding NCAs to EIOPA’s 2023 Consumer Trends work noted that EU consumers are increasingly knowledgeable about pension

EIOPA's work – addressing high costs

Opinion on costs for IOPRs and value for money work

Opinion on costs	▪ Annual costs and charges of 1% of assets may reduce pension income by more than 20% after 40 years of pension saving. Therefore, in order to protect members and beneficiaries, a transparent and comprehensive view of all costs and charges is essential for IORPs, social partners and supervisors ▪ It classifies costs and defines them by grouping them in terms of investment costs, transaction costs, administrative costs, sponsor costs ▪ It includes a report and collection template to increase transparency ▪ Overall high costs necessarily bad – there needs to be value for money ▪ Benchmarks IORPs costs can help in identifying inefficiencies ▪ NCAs should dialogue with IORPs and address high costs/inefficiencies
Value for money work	▪ While the principles are similar in the area of value for money for IBIPs EIOPA has carried out further work to ensure no undue cost is charged to consumers ▪ The manufacturer has sufficiently established that the costs are proportionate compared to market standards, to the type of service provided and to the target market's needs, objectives and characteristics ▪ EIOPA forthcoming methodology on benchmarks aims at promoting a more risk-based approach to supervision and tackling further value for money issues in the IBIPs market

November 2021: Value for money supervisory statement

October 2022: Value for money supervisory Methodology

Forthcoming: methodology to develop value for money benchmarks

THANK YOU!

For more information visit:
https://www.eiopa.europa.eu

European Insurance and
Occupational Pensions Authority

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The French case

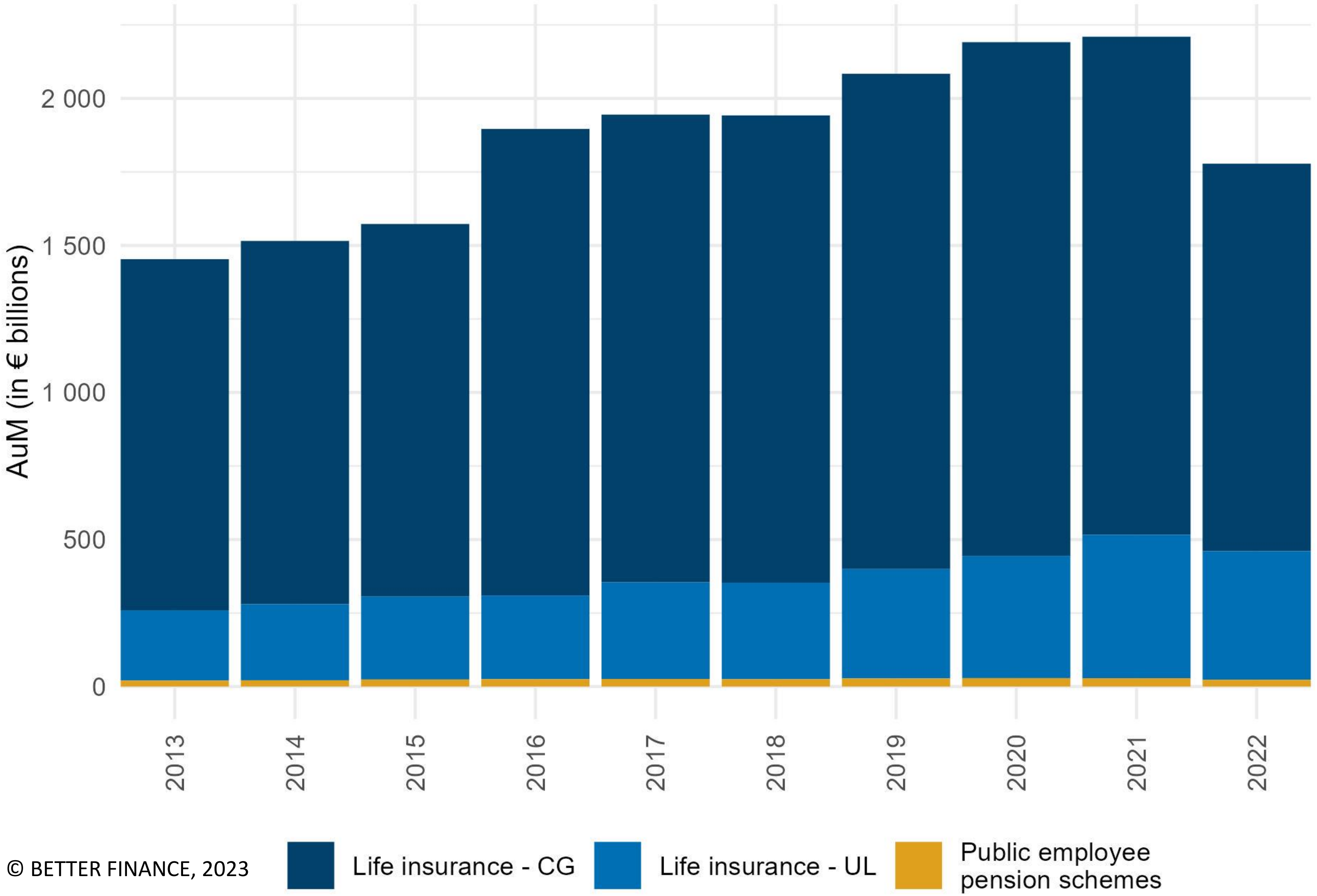
Guillaume PRACHE, Founder & Senior Advisor, BETTER FINANCE
Brussels, 30 Nov. 2023

French financial savings

Financial assets of French households at the end of 2022		
	% of total	**2022/2021**
Currency and bank deposits	35.26%	9.00%
Investment funds*	4.76%	10.10%
Life insurance and pension funds	33.21%	-8.12%
Direct investments (direct holdings of bonds and stocks)	26.76%	-1.53%
Total	***100.0%***	

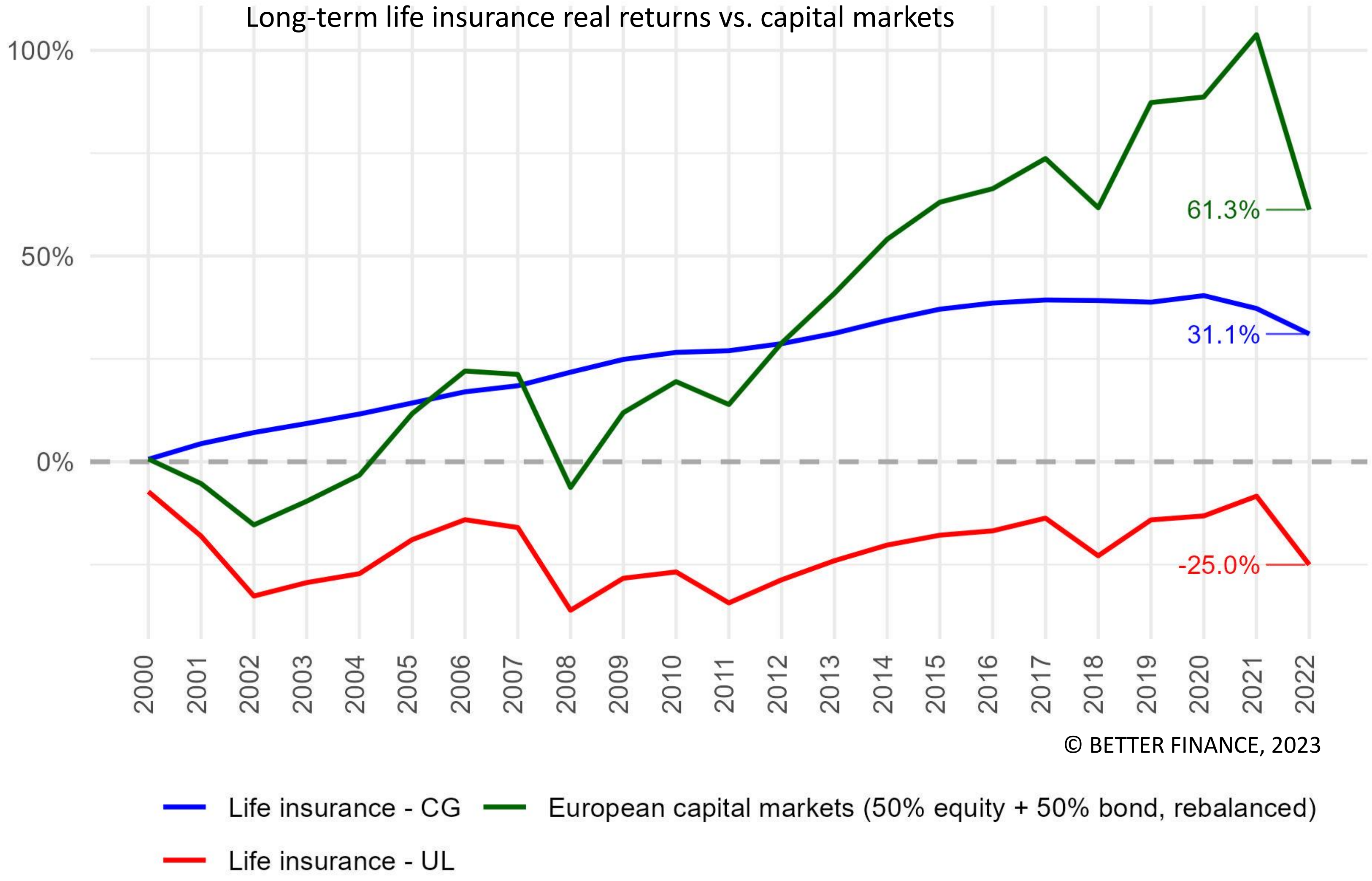
Data: Banque de France
* 10,2% when including "units" of insurance-regulated products

French financial long term and pension savings



Data: France Assureurs, Préfon, UMR; Note: AuM of Corporate long-term and pension savings plans, amounting to €162.2 billion in 2022 are not shown in the graph due to lack of historical data.

French life insurance long term real returns (end 1999 - end 2022)



Data: France Assureurs, GVfM, Eurostat; Calculations: BETTER FINANCE; Details regarding the calculations of the European capital markets benchmark are provided in the introductory chapter of this report.

French Unit-linked insurance poor long term returns
The example of French equity units

French retail market - French equity "units"

(funds sold via insurance contracts = 2/3 of the FR retail fund market)

	Market share	Average charges (unit + contract)	Net nominal performance 2018-2022 (5Y)	Net real performance
Classic units	89,8%	2,90%	0,8%	-11,8%
Clean Share units	0,6%	2,01%	11,5%	-2,4%
Index ETF	1,6%	1,10%	29,1%	13,0%
Index ETF bought directly	-	0,25%	38,9%	21,6%

Sources: GoodValueforMoney.eu, BETTER FINANCE

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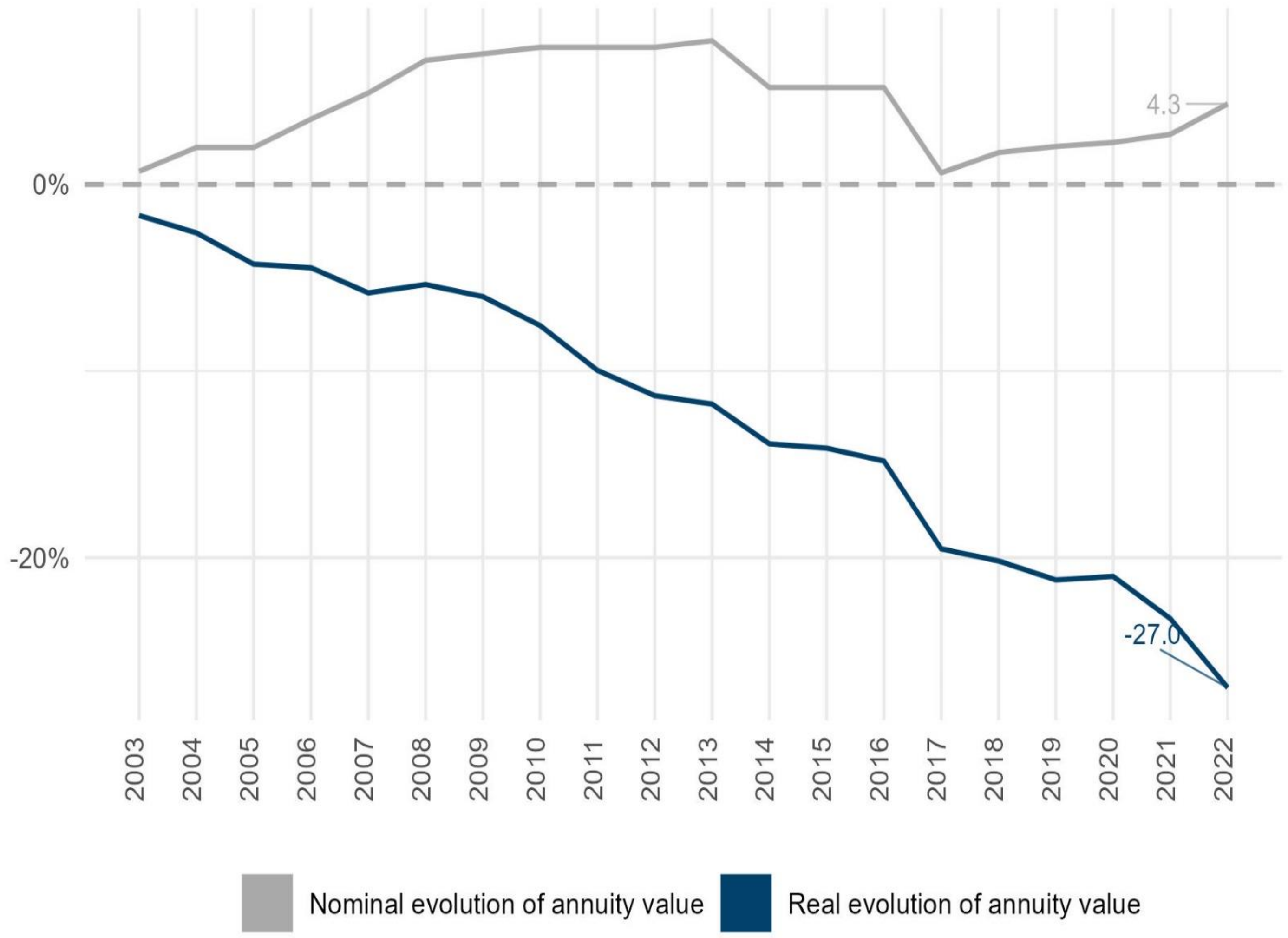
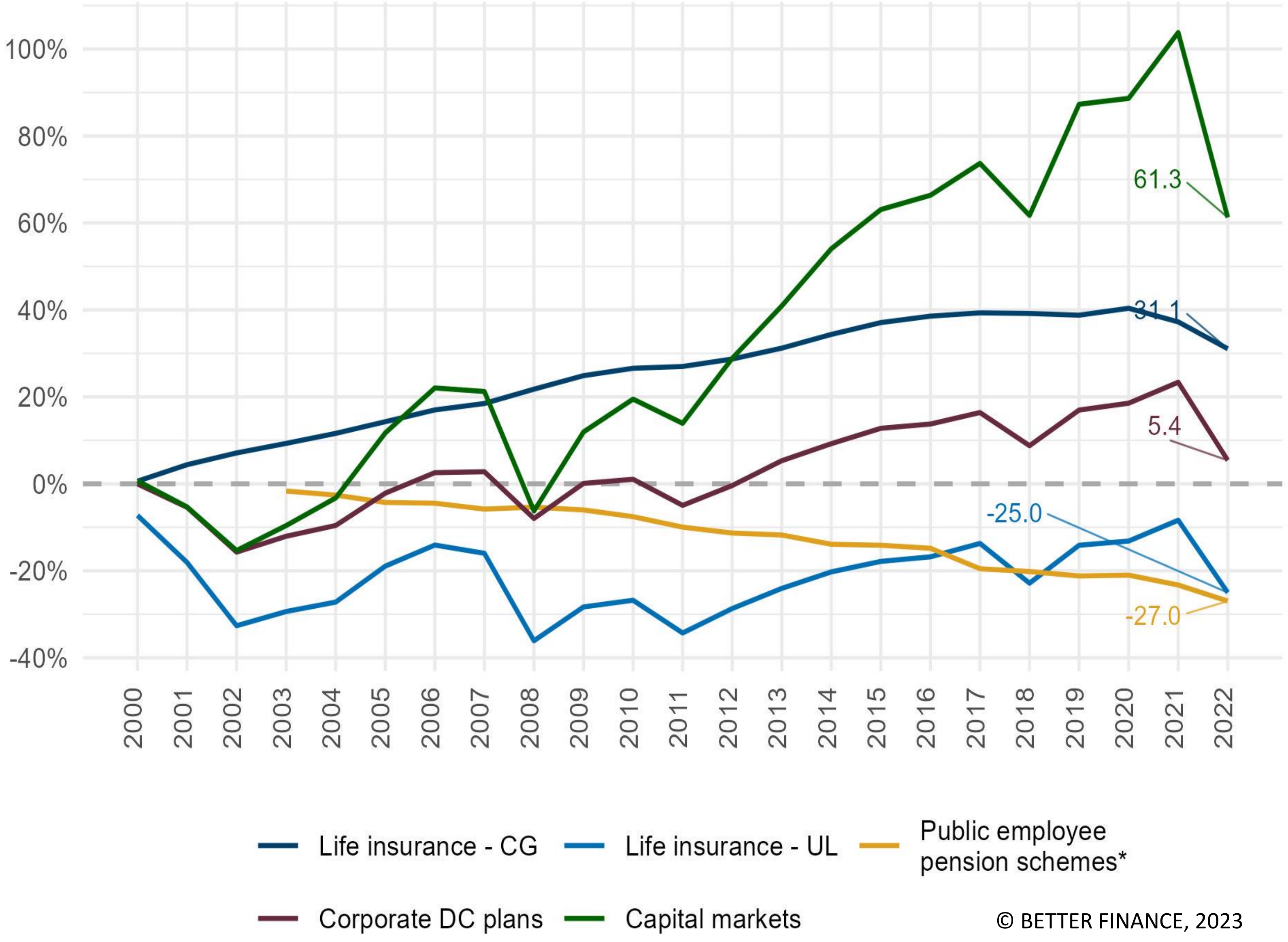
Public employees insurance-based pensions

Compounded evolution of purchasing power of annuities



Data: Préfon, UMR; Calculations: BETTER FINANCE; Note: Purchasing power of annuities is adopted as a proxy for returns; Figures represent the asset-weighted average evolution of Préfon and COREM pension annuities.

Cumulated real returns of French long-term and pension vehicles



Data: France Assureurs, Préfon, UMR, AFG, Eurostat; Calculations:BETTER FINANCE; * Purchasing power of annuities used as proxy for returns of public employee pension schemes

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Thank you for your attention

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Best-in-class:
The Swedish Case

Johan Florén, Chief ESG and Communication Officer, AP7

Brussels, 23 Nov. 2023

PENSIOEN FEDERATIE

PF

Dutch transition from DB to DC

Matthies Verstegen, Head of Brussels Office, Dutch Federation of Pension Funds

The starting point

Features of the current multi-pillar system	
Net replacement rate	Close to 90%
Poverty in old age	3%
Coverage of the second pillar	85% of employees
Pension fund assets	≈1500 bn EUR
Mercer ranking	#1
Current pension contract	DB, nominal promise, conditional indexation or benefit reduction, no sponsor support

Sources: OECD, DNB, Mercer

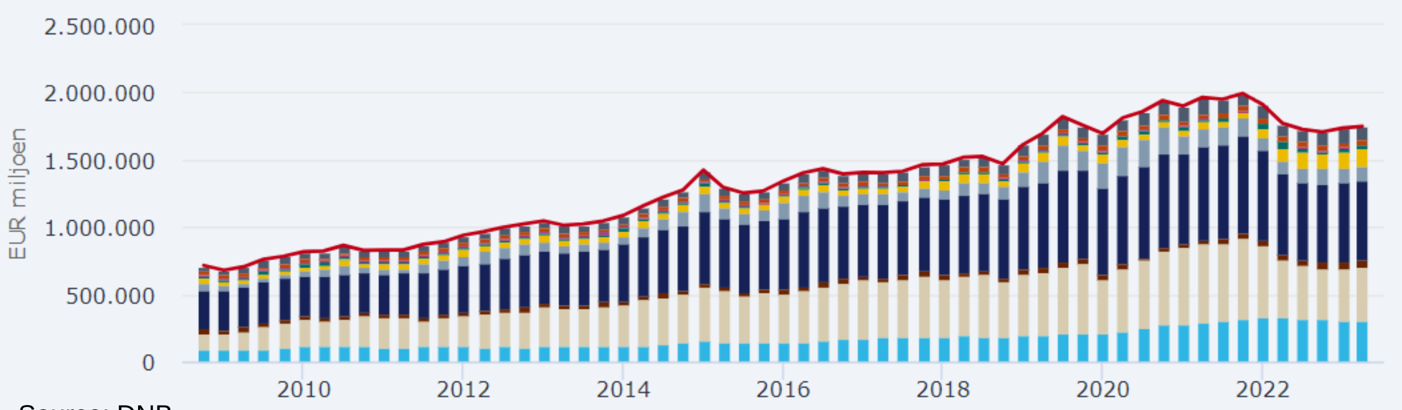
Why change?

- Trust in the system
- Changing labour market

Coverage Ratio

Source: DNB

Asset under Management



Source: DNB

Keeping the strong tenets

- Mandatory participation
- Collectivity
- Risk-sharing

What is changing?

- DB accruals are converted into DC capital
- DC accruals become age-dependent
- Two contracts: “solidarity contract” and “flexible contract”
- Most participants will fall under the solidarity contract:
  - Collective investments / no choice
  - Variable annuity
  - Risk sharing through buffer

New features

Risk preference surveys

Choice guidance

Conclusions

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Time will show impact on:

- Trust: hopefully up.
- Returns: shift towards riskier assets?
- Costs: steady at low level.
- Coverage: other measures needed?