PRESS RELEASE

CORONA PENSIONS? AGE Europe, BETTER FINANCE and CFA Institute call for Measures to protect pension contributions, savings and pay-outs

Brussels, 23 April 2020 - The necessary health, quarantine and social distancing measures taken to fight the ongoing Covid-19 pandemic, are taking their toll on economies around the world. This strategy - crucial to the fight - coupled with monetary and budgetary expansions of unseen magnitudes, will have lasting and damaging economic consequences due to the sudden and legally imposed shutdown of our economies.

In the aftermath of the financial crisis, governments, in an attempt to rekindle growth, took on new debt. Central banks have printed money like never before, with their balance sheets ballooning in recent years[1] under the "quantitative easing" or "unconventional monetary policy" labels. Ordinary citizens, individual investors and pension savers, ended up footing the bill, and are likely to do so again.

National governments, European institutions and central banks have now stepped in to try and mitigate the economic fallout from Covid-19 with even more ambitious and far-reaching fiscal and monetary stimulus packages and measures.[2] On the 19th March 2020, the European Central Bank (ECB) announced a €750 billion Pandemic Emergency Purchase Programme[3] (in addition to the €120 billion already decided on the 12th of March[4]) which will help bolster the numerous initiatives implemented at the national level of EU Member States. This does not include some €3 trillion in ECB refinancing operations at the lowest interest rate ever of -0.75%. This amounts to a vast, disguised but direct, subsidy from the ECB to European banks, as it will actually pay banks to lend them money at the rate of billions of euros per year.

Alas, as with the financial crisis, European citizens as savers and investors (i.e. the middle classes) are likely to disproportionately pay the price once again.

This brings us to the economic concept of "*financial repression*", the result of policies implemented by governments and central banks during the last crisis and highly likely to be implemented to deal with the new Covid-19-induced economic crisis that's facing us. Governments will be even more desperate to find investors to buy bonds with negative or very low interest rate. The least conspicuous Financial Repression method to achieve this, is to get central banks to massively purchase sovereign bonds on secondary markets through the quantitative easing campaigns we are now familiar with. The current prudential rules for banks and insurers may de facto push them to buy negative yielding securities.

[1] The amount of EU Sovereign Debt owned by the ECB increased by 146% from 2009 to 2019. The annual consolidated balance sheet of the Eurosystem comprises assets and liabilities of the Eurosystem national central banks (NCBs) and the ECB held at year-end vis-à-vis third parties: https://www.ecb.europa.eu/pub/annual/balance/html/index.en.html
[2] https://www.investopedia.com/government-stimulus-efforts-to-fight-the-covid-19-crisis-4799723
[3] https://www.bruegel.org/2020/03/coronavirus-and-the-politics-of-a-common-fiscal-instrument/
[4] https://www.ecb.europa.eu/press/blog/date/2020/html/ecb.blog200319~11f421e25e.en.html

Four issues arise for pensions:

- Mandatory **public pension ("pay-as-you-go") systems will be further strained** because of the risk of an unprecedented rise of unemployment and increased budgetary burden faced by EU Member States. Their essential role in ensuring an adequate old age income for all should be protected as recommended by the EU High Level Group on Pensions[5]
- **Worldwide and European equity markets have collapsed** (as of 14/04/2020, MSCI World and STOXX All Europe were down 18% and 22% compared to 14 February) and will probably take quite some time to recover. This has an immediate and direct impact on nearly all pension products. Adding further damage, national governments and the ECB are now calling for the suppression of dividends, as well as allowing issuers of listed equity to hold closed-door general meetings this year, thereby depriving shareholders of several fundamental rights. So much for all the policy talk about shareholder engagement and corporate governance!
- With interest rates at historical lows (sometimes even negative), the vast Corona-induced fiscal and monetary stimulus packages no longer leave a doubt to the fact that **financial repression is here to stay and will deepen, with negative or close to zero real interest rates becoming the norm for many years to come**.
- This unprecedented money creation, combined with tensions in the logistics chains that are developing right now, are **likely to generate a significant upsurge in inflation, further eroding the purchasing power of pension savings and income**.

The pensions time bomb is already ticking in Europe, with studies by BETTER FINANCE and the OECD demonstrating that recent real returns on long-term investments were already too often negative, and insufficient for an adequate replacement income upon retirement.[6] **Real (after inflation) pension returns will collapse this year,** mainly because of stressed equity markets but also because of the low interest in government bonds, and will struggle in the near future because of financial repression, and possibly even more so if combined with resurgent inflation.

BETTER FINANCE had already advocated for several actions to tackle the overall poor long-term real returns of pension savings in the EU - including via the EU's Capital Markets Union initiative - and it is worth remembering to:

- **Make sure that all financial users have access to all markets, including capital markets**. CFA Institute recently released a research study analysing how defined contribution plans are pressured to look for yield into private investments, with potential risk in terms of the liquidity imbalance and return expectations.[7] This requires a return on the capital invested in the shape of either dividend payments or increases in the share price. Dividends are essential to the livelihood of most pension schemes; therefore, the state should not prohibit these payments unless the company is badly hit by the Corona-crisis and has liquidity problems or has received public relief funding.
- **Enable employee share ownership programs** in the next 24 months including tax reductions. Currently personnel-related expenses are the main reasons for the reduced

[5] https://ec.europa.eu/transparency/regexpert/index.cfm?do=groupDetail.groupMeetingDoc&docid=38547
[6] https://betterfinance.eu/wp-content/uploads/PR-PENSIONS-INADEQUACY-25092019.pdf
[7] https://www.cfainstitute.org/en/advocacy/policy-positions/capital-formation-investing-pension-contributions-in-private-markets

liquidity in companies. If such programs were to be introduced immediately, a portion of the salaries could remain in companies as a capital contribution by employees. This could work well if it is linked to tax advantages.

- **End biased advice in "retail" distribution and strongly curb "inducements"** in MiFID 2 and in IDD-regulated investment products. Ensure that financial professionals take their responsibility of offering adequate investment solutions for individual investors based on a duty of care towards their clients, at all times acting in their best interest.
- **Enhance financial literacy**, not for individual investors to determine the best products for them, but to make sure they can choose the adequate level of advice for them. Individual investors lack the necessary knowledge, financial literacy and time to fully understand the exceedingly complex financial products offered to them. Nor should they have to.
- **Fight "greenwashing"** in the design and promotion of ESG investment products.
- **Stop penalising long-term equity investments** versus sovereign bonds in prudential rules.
- ESAs to enforce EU Law by ensuring EU individual investors have full access to low fee investment products such as shares, bonds and index ETFs.
- **Restore standardised disclosure of past performance** (relative to the managers' benchmarks) and costs for all retail investment products.
- Ensure that the future PEPP, the proposed Pan-European Personal Pension product, is really simple, safe and efficient. This also requires EU Member States ensuring there is a level playing field on tax issues, to the extent that this is possible.
- ESAs to improve and continue reporting on costs and past performance of retail investment products.
- ESAs to build a publicly available database where pension products can be compared.

Assuming these actions are taken into account, they will be essential, but insufficient, to cope with this unprecedented crisis. Policy makers and other stakeholders in the pension services field, starting with citizens as pension savers, must design exceptional protective measures to ensure a decent pension income for EU citizens, for now and for the near future. BETTER FINANCE is ready to actively participate in this necessary and urgent process and provide insights and evidence from its long-standing research.

For example, in the past, some Member States guaranteed a minimum annual uptick in the life annuities provided by pension products in order to protect pensioners from the devastating impact of inflation on the purchasing power of pension income.

Today, it is even more important for BETTER FINANCE to reiterate its calls and requests to improve returns on long-term savings (i.e. at least the protection of the purchasing power of these lifelong savings at the time of retirement). After all, in the words of the European Commission, **the priority is an economy, and therefore capital markets, that work for people**.

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