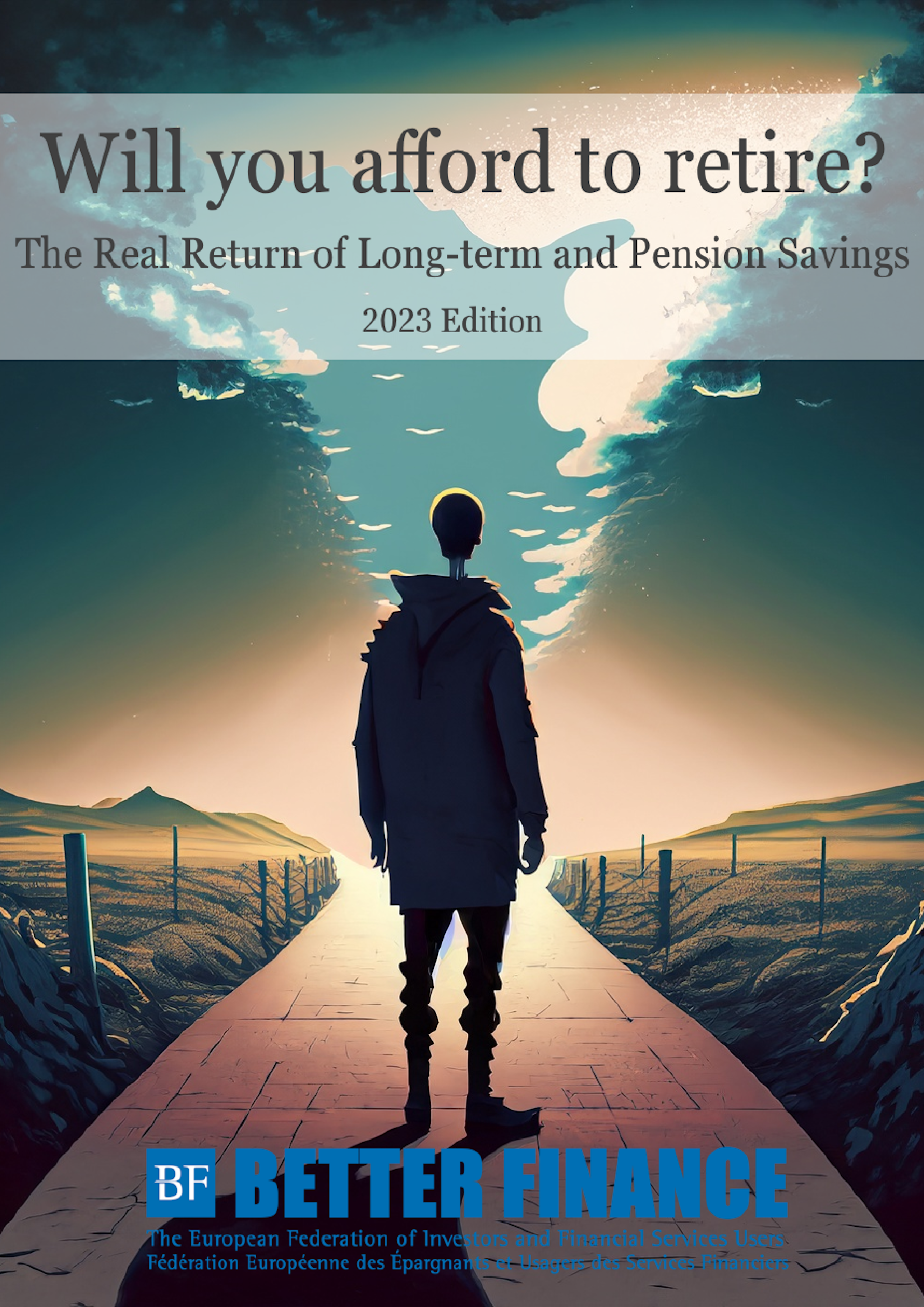
Will you afford to retire?

The Real Return of Long-term and Pension Savings

2023 Edition



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Country Case 9

Italy

Sintesi

Il sistema pensionistico italiano rimane essenzialmente organizzato attorno al suo pilastro pubblico: la pensione statale costituisce il reddito pensionistico primario e spesso l'unico; i fondi pensione complementari coprono solo una minoranza della forza lavoro italiana. Tuttavia, l'invecchiamento della popolazione e i livelli strutturalmente elevati di debito e deficit pubblico mettono a dura prova il sistema pensionistico pubblico: Una serie di riforme ha cercato di limitare l'aumento delle passività pensionistiche dello Stato e di sviluppare schemi pensionistici professionali e individuali a capitalizzazione come alternativa credibile. Queste riforme, tuttavia, non sembrano convincere gli italiani, che investono ancora relativamente poco dei loro risparmi nei fondi pensione contrattuali o aperti, o nei PIP "nuovi", i principali strumenti di risparmio previdenziale che analizziamo in questo capitolo. L'analisi della performance di lungo periodo di questi prodotti sembra dar loro ragione: Su un periodo di 23 anni (2000–2022), i fondi pensione contrattuali e i fondi pensione aperti riescono a offrire solo un rendimento reale netto dello 0,3 e dello 0,6 per cento, mentre le due principali categorie di PIP, i piani "with profit" e i piani unit-linked, mostrano un rendimento reale netto rispettivamente dello 0,3 e dello 0,4 per cento su 15 anni (2008–2023). Un'allocazione eccessivamente conservativa degli asset e—con la relativa eccezione dei fondi pensione contrattuali—costi elevati appaiono come i principali fattori di sottoperformance in termini nominali. L'inflazione a lungo termine si ripercuote poi su ciò che resta delle pensioni private italiane.

Summary

The Italian pension system remains essentially organised around its public pillar: the State pension constitutes the primary and often the only retirement income; complementary pension funds only cover a minority of the Italian labour force. However an ageing population and structurally high levels of public debt and deficit put an increasingly unbearable strain on the public pension system: A series of reform have sought to limit the increase in State pension liabilities and develop funded occupational and individual pension schemes as a credible alternative. These, however, do not seem to convince the Italians, who still invest relatively little of their savings into contractual or open pension funds, or "new" PIP, the main pension saving vehicles that we analyse in this chapter. The analysis of the long-term performance of these products seems to prove them right: Over a 23 year period (2000–2022), contractual pension funds and open pension funds only manage to offer a 0.3% and -0.6% real net return, and the two main categories of PIP, the "with profit" and unit-linked plans, show a real net performance of 0.3% and -0.4%, respectively, over 15 years (2008–2023). An excessively conservative allocation of assets and—with the relative exception of contractual pension funds—high costs appear as the main drivers of underperformance in nominal terms. Long-term inflation then takes its toll on what remains of Italian private pensions.

Real returns 2022

Contractual pension funds: -19.71%

Open pension funds: -20.51%

Introduction: The Italian pension system

In this chapter about Italian private pensions, we will analyse the four product categories listed in Table IT.1. Within the occupational pillar, we will analyse separately the returns obtained by contractual pension funds and open pension funds over 23 years (2000–2022). Our reporting period will be shorter for *Piani Individuali Pensionistici* (PIP), the individual pension plans constituting the third pillar of the Italian pension system: we will analyse performance since 2008, distinguishing between PIP "with profit" and unit-linked PIP.

Table IT.1 – Long-term and pension savings vehicles analysed in Italy

Product	Pillar	Reporting period *Earliest data*	*Latest data*
Contractual pension funds	Occupational (II)	2000	2022
Open pension funds	Occupational (II)	2000	2022
PIP with profits	Voluntary (III)	2008	2022
PIP unit-linked	Voluntary (III)	2008	2022

Like for most European savers, 2022 was a terrible year for Italians. As shown in Table IT.2, the 1-year returns after charges and inflation of three of the four product categories constituting the Italian private pension system fell close to or below -20%. The long-term performance of Italian private pensions, while less catastrophic, is still disappointing, with two product categories in negative territory.

Table IT.2 – Annualised real net returns of Italian long-term and pension savings vehicles (before tax, % of AuM)

	Contractual pension funds	Open pension funds	PIP with profits	PIP unit-linked
Reporting period	2000-2022	2000-2022	2008-2022	2008-2022
1 year (2022)	-19.7%	-20.5%	-9.9%	-21.2%
3 years (2020–2022)	-5.8%	-5.7%	-3.8%	-5.6%
5 years (2018–2022)	-3.0%	-3.1%	-2.0%	-2.8%
7 years (2016–2022)	-1.6%	-1.7%	-1.1%	-1.4%
10 years (2013–2022)	0.3%	0.5%	0.0%	0.9%
Whole period	0.3%	-0.6%	0.3%	-0.4%

Data: COVIP; *Calculations:* BETTER FINANCE.

In the remainder of this section, we will briefly present the Italian pension system, including its Pillar I State pension, before delving into our analysis of the four private pension categories. We will then report on the costs and charges levied on savings accumulated in these products, the fiscal regime applicable to them, before analysing their performance over the reporting period.

Pension system in Italy: An overview

The Italian pension system is organised around the classic three-pillar World Bank model:

- Pillar I is a public pension scheme managed by the Italian State;

- Pillar II is composed of occupational pension arrangements, to which enrolment is mandatory;
- Pillar III is composed of individual pension saving products, subscribed on a voluntary basis.

Both Pillar II and Pillar III pension funds and plans are supervised by Commissione di Vigilanza sui Fondi Pensione (COVIP), whose data constitutes the basis of our analysis of costs and performance.

Pillar I: The State pension

The first pillar remains the main pension vehicle in Italy. It is composed of two tiers: zero and first. The zero tier consists of a social pension ensuring a minimum level of income for the elderly. The first tier covers employed individuals and for those who entered the labour market before 1995, functions as a DB system. The "Dini reform" of 1995 however changed the nature of the first tier for all those who entered the labour market after 1995: the system is now organised as a notional defined contribution (NDC) system and pension entitlements are no longer computed according to an earnings-related system (Riforma del sistema pensionistico obbligatorio e complementare (legge 335/1995), 1995).

Further reforms and adjustments of the Italian public pension system were adopted in the 2010s, in order to restore sustainability, in the context of an ageing population and massive pension expenditure. In 2011, Esla Fornero, minister for Welfare and Social Policy under Mario Monti's "technical" government, implemented a reform intended to bring the system close to equilibrium. The main eligibility criterion became the number of years worked rather than one's age, with early retirement legally possible but subject to penalties. Nevertheless, the Italian Constitutional Court stated in April 2015 that the suppression of indexation of pensions on inflation included in the "Fornero law" was unconstitutional: the indexation of pensions on inflation was estimated to add € 500 millions to the costs of the State pension.

This judicial reversal was succeeded by the adoption of measures facilitating early retirement, such as the "Ape Sociale", "Opzione Donna" and, most notably, the "Quota 100" measure, effective from January 1, 2019. This measure enables employees with a minimum of 38 years of service to retire early if the combined total of their age and years of service reaches 100. The "Quota 100" has since been reviewed, becoming "Quota 102" in 2022 and may be revamped again as "Quota 103" or even "Quota 104" (41 years of contributions and 63 years of age) in the reform announced by Giorgia Meloni's government for 2024. The government—under the pressure of a high public debt and deficit as well as inflation—seeks to reduce the opportunities for early retirement, but faces the opposition of trade unions, supported on this occasion by the right-wing *Lega Nord* party (Rogari, 2022).

Pillar II: Occupational pensions

The second pillar of Italian pensions is composed of collective complementary pension plans. These can be contractual occupational pension funds—managed by social partners under collective bargaining agreements (CBAs)—or "open" pension funds constituted by various types of financial institutions, which welcome members on an individual or collective basis (Commissione du Vigilenza sui Fondi Pensione [COVIP], 2022).

Besides pension funds, the *Trattamento di Fine Rapporto* (TFR) is also part of the second pillar. The TFR is a deferred indemnity: each year the employer is required to set aside a portion of the employee's salary, to be accumulated and returned to the employee upon termination of the employment contract.

Pillar III: Voluntary individual pensions

The third pillar is composed of voluntary contributions to individual complementary pension schemes, PIP. Individuals can also make contributions to open funds in the case of individual affiliations. Given the strong component of mandatory contributions within the state pension system, both collective and individual complementary pension funds play a small role in the financing of future retirees' income. While the savings in collective complementary pension funds are rather small, private savings are still consistent. If all pension contributions and home ownership were transformed into an annuity, the corresponding stream of generated income at retirement would be very high.

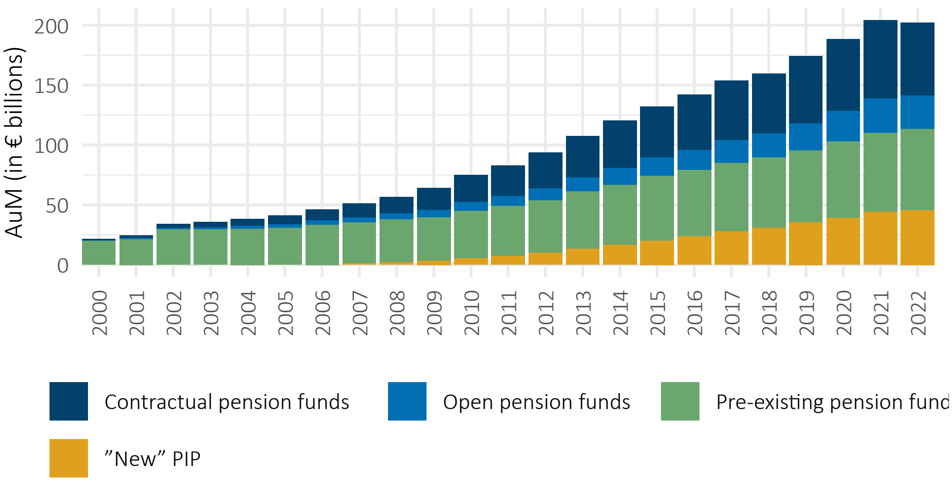
To summarise the information of the pension system set-up and to obtain a basic overview of the pension system in Italy, the table below presents key data on the multi-pillar pension system.

Long-term and pension savings vehicles in Italy

At the end of 2022, 9.1 million Italians were enrolled into at least one collective or individual pension plan (Pillar II or III), covering 36.2% of the working population (COVIP, 2023). This represents an increase of 650 thousand employees from end-2021. The contractual pension funds had the strongest increase in members (+9.9%) as well as in net contribution collection (+17.44%).

As shown in Figure IT.1, the share of "pre-existing" funds in the total AuM of Italian private pension vehicles shrinks over time, while contractual pension funds and "new" PIP are becoming the main pension savings vehicles.

Figure IT.1 – AuM of Italian long-term and pension savings vehicles



Data: COVIP; *Calculations:* BETTER FINANCE; *Note:* Available AuM data for "new" PIP does not differentiate between with-profit and unit-linked contracts.

Table IT.3 – Overview of the Italian pension system

Pillar I	Pillar II	Pillar III
State pension	Occupational funded pension	Individual funded pension
"Dini law" (1995) and "Fornero law" (2011)	Legislative Decree 124/93 on complementary pension plans implemented in 1993, and Reform on complementary pension (Legislative Decree 252/2005)	
Instituto Nazionale Previdenza Sociale (INPS)	Pension accumulation companies	Insurance companies and other financial institutions
Mandatory	Voluntary	Voluntary
Publicly managed	Privately managed	Privately managed
PAYG	Partially or fully funded	Fully funded
notional defined contribution (NDC)	DC	DC
	Quick facts	
Number of old-age pensioners: 10.7 mln.[a]	Funds: 264	Funds (new PIP only): 68
Average old-age pension: € 1 393	AuM: € 89.14 bln.	AuM (old and new PIP): € 51.3 bln.
Monthly household average income (net): € 2 492	Participants in 2022: 6.1 mln.	Participants in 2022: 3.8 mln.
Aggregate replacement ratio (2022):75%[a]	Coverage ratio: 24.4%	Coverage ratio: 15.0%

Data: (COVIP, 2023);

[a] Eurostat data (the number of old-age pensioners excludes pension survivors and anticipated old-age pensions).

Over the past twenty-three years covered in our report, the number of pension funds and plans on offer in Italy was reduced dramatically: From 739 funds and plans in operation in 1999, only 332 remained active in 2022. As the supervisor, COVIP explains:

> The reduction in the number of pension forms operating in the system, especially for pre-existing funds, is primarily driven by concentration in the financial sector, which led to the formation of banking and insurance groups within which several supplementary pension schemes dedicated to employees of individual banks coexisted. Schemes dedicated to the employees of individual banks and insurance companies later merged into these groups. In many cases, the ensuing reorganisation process led to the concentration of the pension schemes of individual companies in one or two group funds, separated according to the type of scheme. (COVIP, 2023, p. 16)

The concentration trend particularly affected the "pre-existing" funds, and to a lesser extent contractual and open pension funds. The number of "new" PIP, individual pension plans introduced in 2007, remained relatively stable.

Complementary pension funds were introduced in 1993 and are composed of contractual funds, open funds and individual pension plans provided by life insurance companies. The main features of complementary pension plans are:

- Membership is voluntary;
- Pensions are funded;
- Schemes are managed by banks, insurance companies or specialised financial institutions;
- Their supervision is ensured by COVIP.

Following the signature of a CBA, all complementary pension funds are managed by an external financial institution that can only be an insurance company, a bank or a registered asset management company (Legislative Decree 252/2005). All complementary pension funds now operate on a DC basis, as this is the only permitted type of pension plan.

DB plans are restricted to older funds, that existed before the transition to the DC model ("pre-existing" funds). The budget law of December 11, 2016 allows members of complementary defined contribution pension funds, who are close to retirement age, to receive early retirement income from their accumulated savings in whole or in part; the scheme is called *Rendita Integrativa Temporanea Anticipata* (RITA). Eligible employees are those who benefit from a similar provision in the first pillar, the *APE Sociale*. To be eligible for RITA, an individual must:

- cease their professional activity;
- reach the requirements necessary to receive the old-age pension in their mandatory regime within the next five years or to be unemployed for more than 24 months;
- have contributed at least 20 complete years to the mandatory regime; or / and have completed five years in the pension scheme.

The individual determines the amount of the accrued capital to use until their official retirement. The RITA is also offered to people who have been unemployed for at least two years before their request for withdrawal and are within ten years of the statutory retirement age.

In 2022, a total of € 1 643 million was paid out of Italian private pensions under RITA, € 357 million more than in 2021. The average withdrawal amounted to € 57 000, over a total of 28 800 withdrawals (only 6 100 people withdrew the entire amount).

Second pillar: Contractual and open pension funds

Three types of funds exist within the occupational pillar:

- "Contractual", also called "closed" funds, membership in which is restricted to specific groups of workers;
- "Open" funds, which are open to all;
- "Pre-existing" funds—that is, funds that existed before the Italian legislator regulated the form of Italian private pensions—are still operating and can accept as new members the employees of the firm(s) or economic sector for which they have been established, although no new such fund can be created.

Contractual funds are also called closed funds due to their restrictive membership criteria: only firms of the specific firm, firms or economic sector for which the fund was established can join in. Generally, contractual funds are established for employees whose contract is regulated by a CBA; for the self-employed, contractual funds are usually provided by professional associations, and consequently reserved to their members. At the end of 2022, contractual funds had 3.6 million members, 133 619 of whom were also members of at least one contractual fund, and 297 856 and a "new" PIP.

Contractual funds' assets are legally separated from those of the sponsor company or association, being therefore protected from creditors' claims in case of bankruptcy of the employer. A contractual fund must place its assets under the custody of an authorised depository (bank or investment firm). The fund's Board of Directors is responsible for defining the investment strategy and choosing the investment manager, the depositary bank and the entity designated to administer the pensions. The fund must report at least on an annual basis. Managers' mandates usually last five years or more, in line with the long-term orientation of funds.

Open funds, by contrast, do not restrict membership: they are set up by banks, insurance companies, asset management companies and stock brokerage firms for anyone to join on a collective or individual basis. Employees of the public sector, as well as self-employed and liberal professions can only join on an individual basis; other employees can join individually, but collective membership is also possible where provided for by a company or sectoral agreement. At the end of 2022, open funds had 1.8 million members, 32 298 of which were also members of at least one other open fund and 107 255 had a "new" PIP.

The assets of open pension funds are legally separated from those of the financial companies that set them up and are thus protected, in case of the company's bankruptcy, from the claims of any creditors. Like contractual pension funds, open funds must have an authorised depositary bank and can outsource administration.

Italians benefit since 1982 from the TFR, a severance payment system whereby the employer pays a portion—6.91%—of the employee's annual salary into a specific vehicle for asset accumulation, the TFR. If an employee decides to opt-out of complementary pension funds and belongs to a company with more than 50 employees, their accumulated amount of severance payments is transferred to INPS, the national social security institute, which, by law, manages the severance payment. For an employee who works in a firm with less than 50 employees and who does not opt for complementary pension funds, their TFR remains with the firm they work at and represents a debt for the company.

The accumulated amounts are mandatorily saved and can only be paid upon termination of the work contract (whatever the reason of the termination). In exceptional cases (health issues, first-house purchases, parental leave), the TFR can be partially drawn, up to 70% of the accumulated amount. The TFR is revalued annually at a rate of 1.5% plus a variable part indexed on the national inflation rate calculated by the national statistics office (Istat). In 2022, as a positive side effect of soaring inflation, the TFR's rate rose to 8.3%,

As an alternative, since 2007 and entry into force of Legislative Decree 252/2005, each employee can individually opt to have their TFR paid into a complementary pension fund. For specific sectors where a contractual pension fund exists, tacit consent applies for the TFR to be transferred to the fund instead of remaining with the company.

The introduction of contractual and open funds, and the possibility to place one's TFR with them was a significant novelty in the Italian pension landscape, which had been thus far almost exclusively organised around the State pension. Workers now had to make decisions regarding where and how to invest the portion of their income they wish—or, rather, must—save for future retirement income.

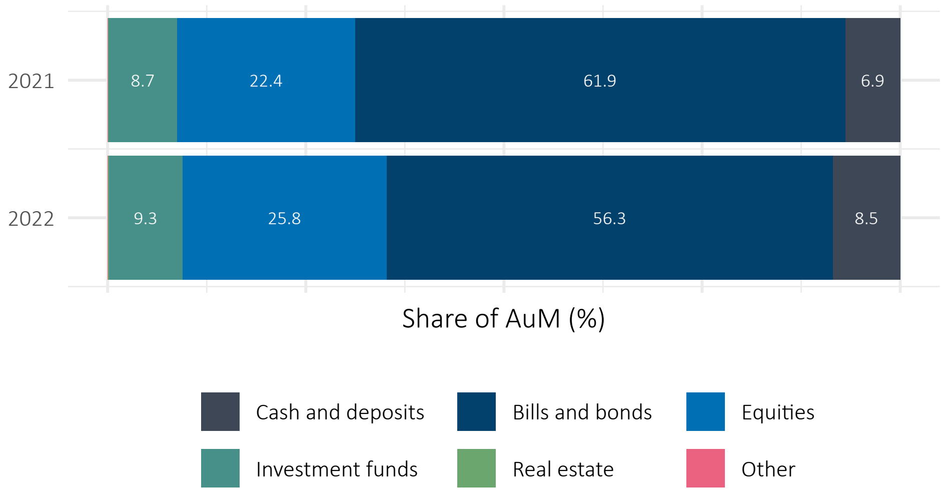
The coverage of public employees by specific retirement products is very limited, as the law introducing pension funds excluded them. Contractual pension funds are only possible for individuals working in National Education (Espero), in the National Health system and in a regional or local authority (Perseo and Sirio). These contractual pension funds were implemented in 1993.

In terms of allocation of pension savers' assets, both contractual and open pension funds implement conservative investment policies, as shown in Figures IT.2 and IT.3 for the years 2021 and 2022. Contractual pension funds invest only a quarter of their assets into equity vs. over 50% in debt securities. Open pension funds are only slightly less conservative, with 30.1% invested in equity and "only" 43.3% in bills and bonds.

Third pillar:

Piani Individuali Pensionistici (PIP) are individual pension plans offered by insurance companies. Their main purpose, according to the Italian committee for financial education includes but is not limited to pension savings: they can also be used to accumulate savings for major projects or unforeseen events . Anticipated withdrawals are therefore possible in case to pay for extraordinary health expenses, for first-home purchase and renovation, or for "personal and family motives", the latter two only after an 8-year holding period (Comitato per la programmazione e il coordinamento delle attività di educazione finanziaria, 2023). An anticipated pension may also be requested as per the RITA framework. Full withdrawals are also possible in case of permanent invalidity, unemployment longer than 48 months, resignation or dismissal and, of course, death of the investor.

Figure IT.2 – Allocation of Italian contractual pension funds' assets



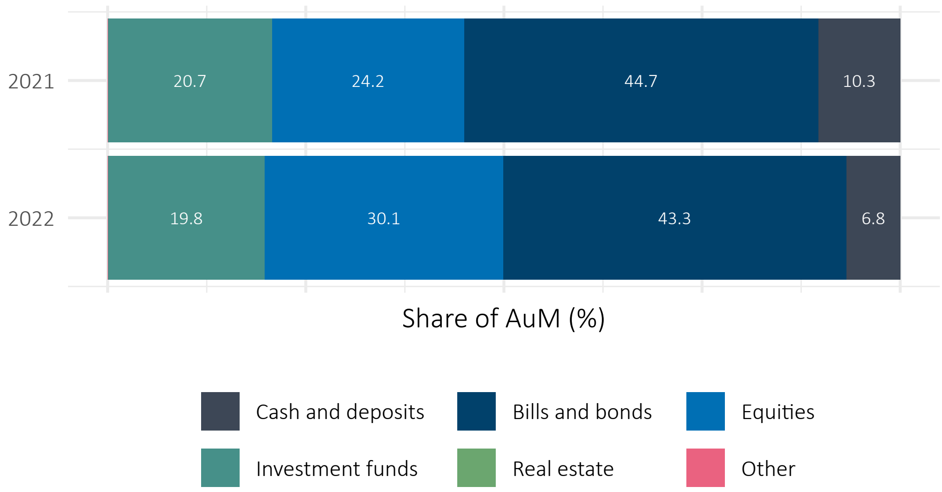
Data: COVIP; *Calculations:* BETTER FINANCE.

Two main types of contracts are offered: *gestione separata* ("with profit", 74.9% of AuM in "new" PIP in 2022) or unit-linked (25.1%). The with-profits policies guarantee a minimum rate of return (guaranteed and consolidated in the company's accounts) which is added to a quota related to the financial performance. The unit-linked policies do not have a guarantee. Their performance depends on the value of the units in which contributions are invested.

Assets are allocated very differently under the two types of PIP, as shown in Figures IT.4 and IT.5. PIP with are massively invested in debt securities (84% in 2022, of which 38.3% in Italian government bonds) and virtually do not invest in equities (2.4%). By contrast, in PIP unit-linked, equity represents more than a third of investments, while debt securities only account for a fourth of AuM.

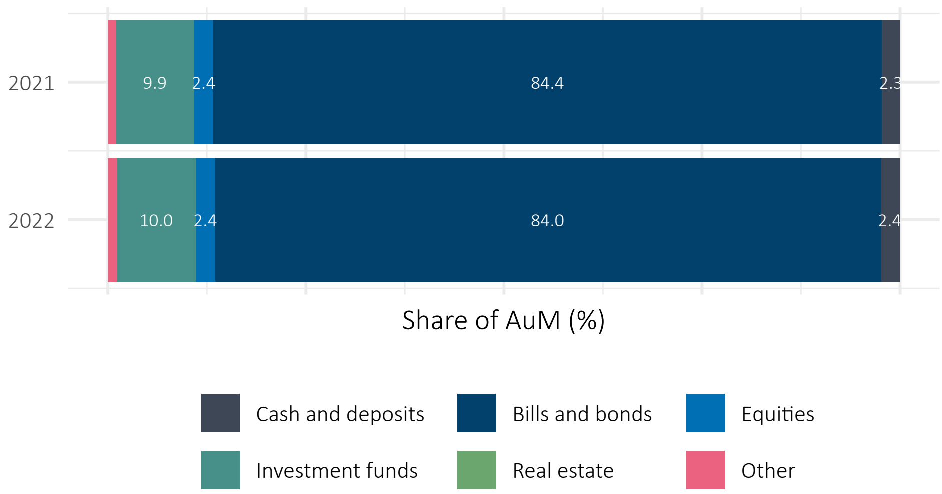
We should further note that the allocation of assets varies within the unit-linked category, where there exists three main sub-types: the *obbligazionaria*, the *bilanciata* and the *azionaria*. The *obbligazionaria* invests close to 70% of assets in government bonds (68.7% in 2022) and nothing in equity. By contrast, in the *azionaria* type, assets are invested for more than 70% in direct equity holdings (71.7% in 2022) and only a tiny fraction of assets are invested in debt securities (4.4% in 2022).

Figure IT.3 – Allocation of Italian open pension funds' assets



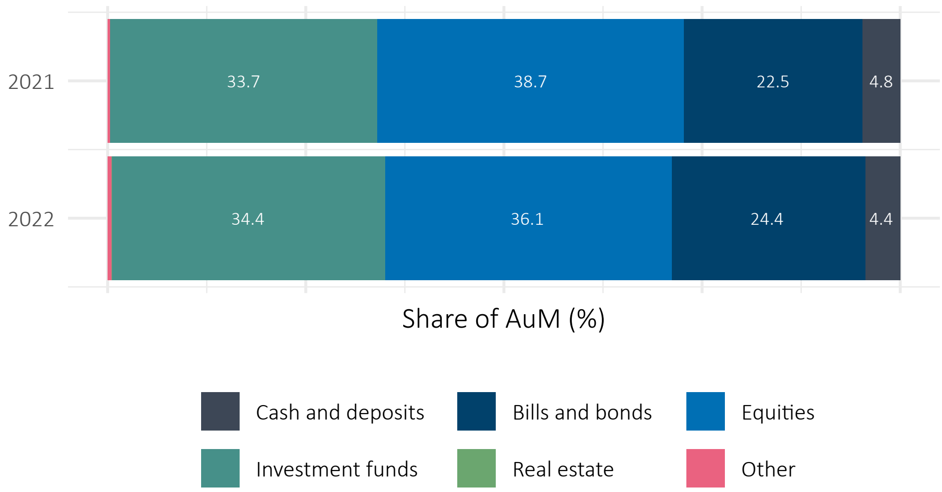
Data: COVIP; *Calculations:* BETTER FINANCE.

Figure IT.4 – Asset allocation of Italian PIP with profits



Data: COVIP; *Calculations:* BETTER FINANCE.

Figure IT.5 – Asset allocation of Italian PIP unit-linked



Data: COVIP; *Calculations:* BETTER FINANCE.

Charges

COVIP calculates a synthetic indicator of costs for a member who contributes € 2 500 every year with a theoretical annual return of 4%, over increasing periods of 2 to 35 years. The calculation methodology of the indicator was revised by COVIP in order to eliminate distortions between the categories of funds. Since 2014, the tax rates on investment revenues depend on the underlying assets of the funds. Since March 2015, the cost indicator is no longer calculated net but gross of the tax paid by pension funds on their revenues. Table IT.4 shows the average, maximum and minimum values of this synthetic cost indicator in 2022.

Table IT.4 – COVIP's Synthetic Cost Indicator

	Synthetic Cost Indicator			
Statistic	2 years	5 years	10 years	35 years
Contractual pension fund				
Mean	1.13%	0.64%	0.47%	0.34%
Minimum	0.21%	0.15%	0.13%	0.07%
Maximum	2.99%	1.52%	1.29%	1.14%
Open pension funds				
Mean	2.32%	1.56%	1.35%	1.23%
Minimum	0.55%	0.55%	0.55%	0.55%
Maximum	4.73%	3.20%	2.58%	2.31%
"New" PIP				
Mean	3.77%	2.62%	2.17%	1.82%
Minimum	1.04%	0.85%	0.58%	0.38%
Maximum	6.44%	4.82%	4.07%	3.44%

Data: COVIP, *Relazione annuale 2022*.

As we can see, there is a great variation among pension funds in terms of costs, both between and within categories of funds. Savers should therefore be very attentive to the cost information provided by fund managers before making investment decisions.

The cost indicator decreases significantly with the membership period, as initial fixed costs are progressively amortised: the drop in average costs between 2 years and 35 years is 0.79 pp for contractual funds, 1.09 pp for open funds, and even 1.95 pp for "new" PIP. In line with the long-term orientation of this report and of pension savers, the cost figures that we retain to calculate net returns of each of the four product categories analysed in this report is therefore the mean value of the synthetic cost indicator for 35 years.

In 2022, the cost indicator for open pension funds remained remarkably stable, equal to the second decimal place to the value for 2021. The average indicator for contractual pension funds increased across all holding periods (+0.02 pp for 2, 10 and 35 years, +0.01 pp for 5 years). The costs of "new" PIP—the most expensive of the three categories—decreased for the shorter periods (-0.02 pp for 2 years) but remained stable for the long-term.

There are significant differences between each category of funds, depending on the distribution channels of the products and the fees paid to distributors. Economies of scale lead to lower costs for closed funds while no such impact can be observed on new PIP and open funds, according to a review of individual figures by COVIP.

Taxation

The taxation regime of pension savings in Italy is essentially an ETT regime (exempt, taxed, taxed), corresponding to the following three stages over time: contribution, accumulation and payment. In the first phase, employee contributions to private pension funds benefit from a favourable tax treatment. Employees can deduct their own contributions from their taxable income up to a ceiling of € 5 164.57 per year. Employer contributions are considered as employment income and are thus subject to tax and social security contributions.

Until 2014, in the second phase a tax rate of 11.5% was applied on the accrued capital gains paid by complementary pension funds. Since January 1, 2015, this tax rate increased to 20%, except for accrued capital gains generated by investments in Government Bonds which are taxed at a rate of 12.5%. The difference in taxation rates of bonds and equities is an incentive to change the asset allocation towards the former, a trend that is likely to lower the returns of pension products in the future. The budget law of December 31, 2016 foresaw that assets invested in European equities or European investment funds (up to 5% of the fund's total assets) were exempted from income tax.

In order to avoid double taxation, benefits are taxed only on the corresponding shares that were not taxed during the accumulation phase. Contributions that were not deducted, and thus already taxed, won't be taxed again.

In the third phase the corresponding benefits are taxed at a rate ranging between 9% and 15%, depending on the length of membership in the private pension funds. Income received before retirement age in the framework of the RITA scheme is taxed at 15%, reduced by 0.3% for each year over the fifteenth year of participation in supplementary pension schemes, with a maximum reduction limit of six percentage points. If years of enrolment in the supplementary pension scheme are prior to 2007, those years can be considered up to a maximum of 15 years. The tax rate of pension benefits that come from TFR varies between 9% and 15%, depending on the length of enrolment in the complementary pension funds.

Table IT.5 – Taxation of pension savings in Italy

Product		Phase		Regime
	Contributions	*Investment returns*	*Payouts*	
Contractual pension funds	Exempted	Taxed	Taxed	ETT
Open pension funds	Exempted	Taxed	Taxed	ETT
PIP with profits	Exempted	Taxed	Taxed	ETT
PIP unit-linked	Exempted	Taxed	Taxed	ETT

Data: Comitato per la programmazione e il coordinamento delle attività di educazione finanziaria (2023).

Performance of Italian long-term and pension savings

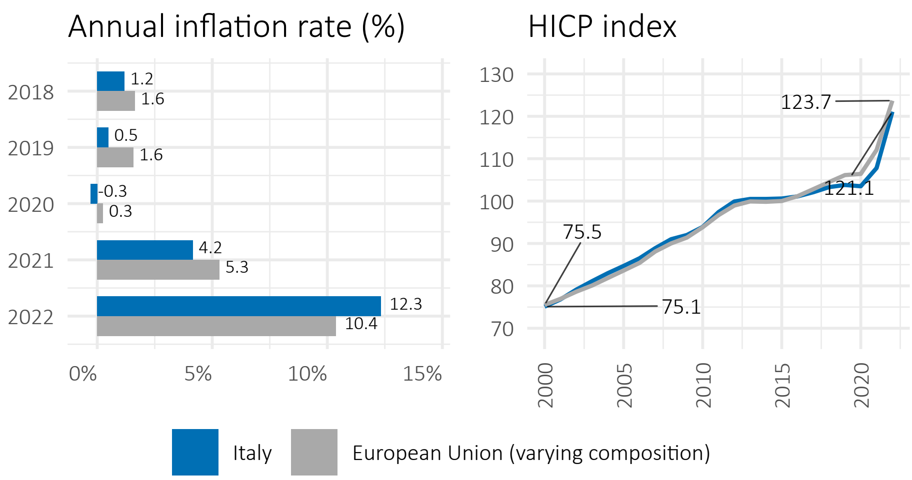
Real net returns of Italian long-term and pension savings

In this section, based on data from COVIP (2023) we analyse the nominal returns obtained by contractual pension funds and open pension funds since 2000 and the two main types of "new" PIP since 2008 (the first full year of operation for these products), and compute *real net returns*, that is, after charges and inflation, over these periods.

Figure IT.6 – Inflation in Italy

Period 2000–2022

	Annualised	Compounded
Italy	2.2%	65.7%
European Union (varying composition)	2.3%	67.5%



Data: Eurostat, HICP monthly index (2015 = 100); *Calculations:* BETTER FINANCE

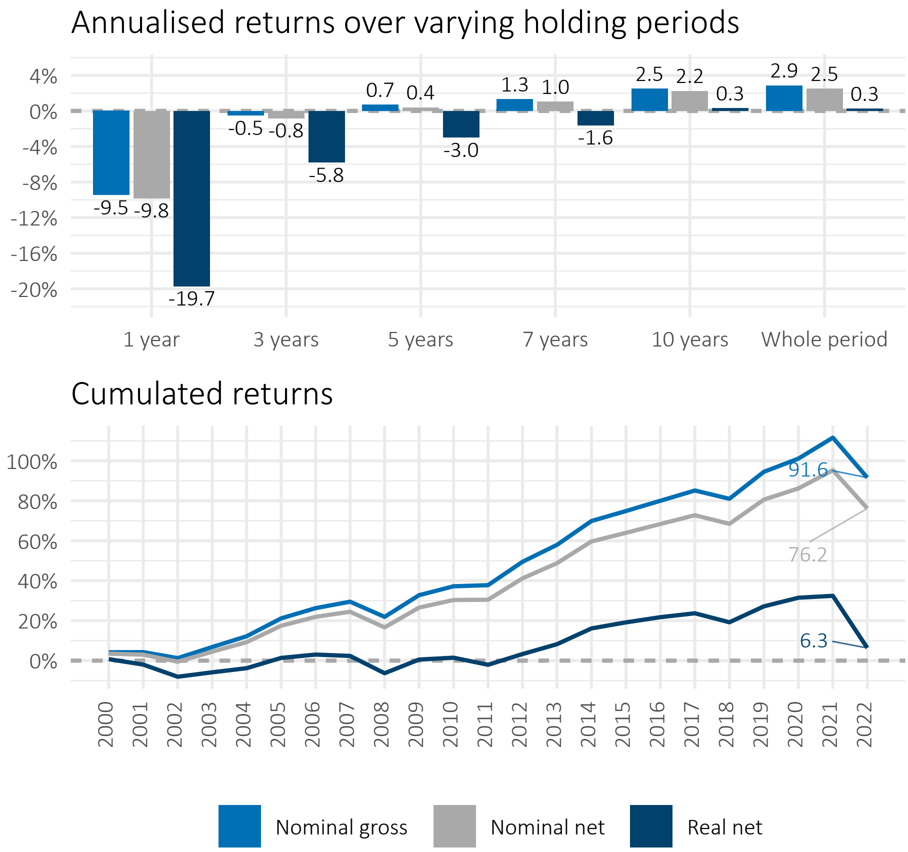
As already mentioned, in order to calculate the long-term net returns, we deduct annual costs from each year's nominal gross return figure. For that operation in the Italian case, we take for each year and each product category the average value of COVIP's synthetic cost indicator for a 35 year period (see Table IT.4).

In order to correct the nominal net returns for inflation, we calculated the annual inflation rate in Italy since 2000, based on Eurostat's HICP (see methodology on Page 6). As can be seen from Figure IT.6, in terms of inflation, Italy was slightly below the EU average over the period 2000-2022, with a 2.2% annual average and a 65.7% cumulated. In 2022, however, inflation climbed to 12.3%, 1.9 pp above the EU average (10.4%).

Performance of contractual and open pension funds

Figures IT.7 and IT.8 show the nominal gross, nominal net and real net returns of contractual and open pension funds. Even before the inflation hike of 2021-2022, the long-term real performance of these products attests to the eroding effect of inflation on investment returns: over 23 years, inflation reduced the cumulated performance of contractual pension funds by 69.9 pp, and that of open pension funds by 56.9 pp, turning the later negative at -13.3%. Therefore, Italian workers who may be under the illusion that the value of their pension savings almost doubled over the past two decades have actually barely gained purchasing power if investing in contractual funds, and actually lost purchasing power if investing in open pension funds.

Figure IT.7 – Returns of Italian contractual pension funds (before tax, % of AuM)



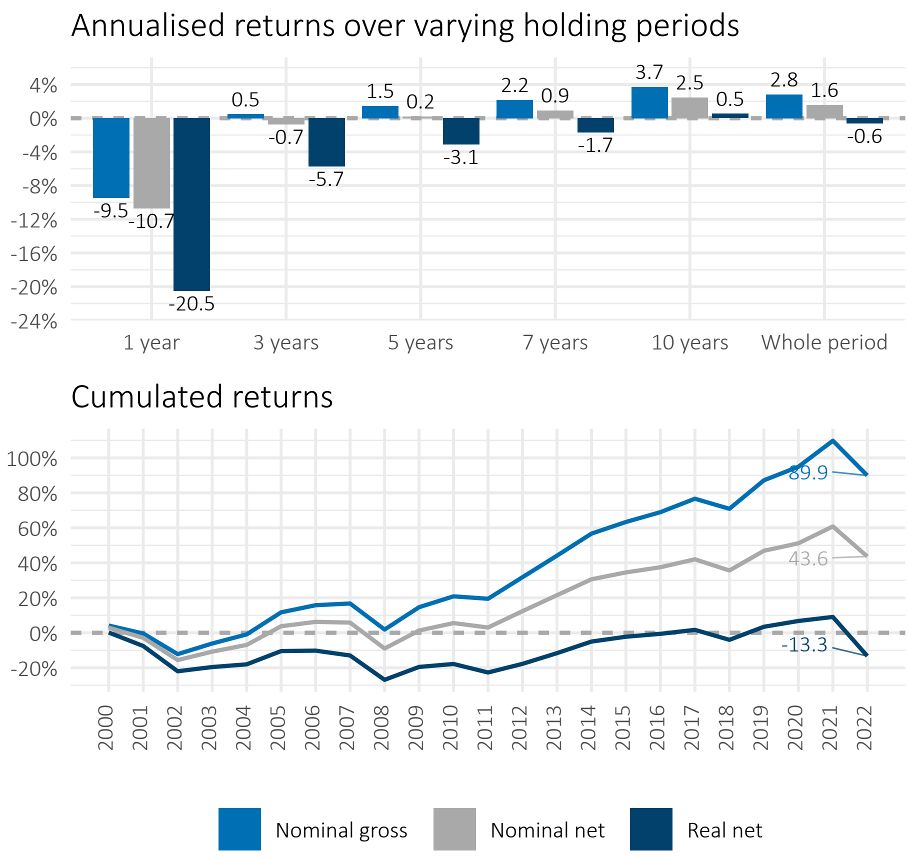
Data: COVIP, Eurostat; *Calculations:* BETTER FINANCE.

The results of open pension funds furthermore show the long-term impact of costs: While nominal returns before charges are similar to those of contractual pension funds, the higher average 35-year synthetic cost indicator of open pension funds (+0.89 pp in 2022), result in a nominal net performance 32.6 pp lower than that of contractual funds.

Performance of "new" PIP

Figures IT.9 and IT.10 painfully show the impact of costs on long-term performance: over half the cumulated performance is eaten away by charges levied on PIP (-42.9 pp for with profit contracts and -38.9 pp for unit-linked ones). The rest of the performance is wiped out by inflation, resulting in a meager +4.4% return for the misnamed "PIP with profits" over 15 years, and even a loss of

Figure IT.8 – Returns of Italian open pension funds (before tax, % of AuM)



Data: COVIP, Eurostat; *Calculations:* BETTER FINANCE.

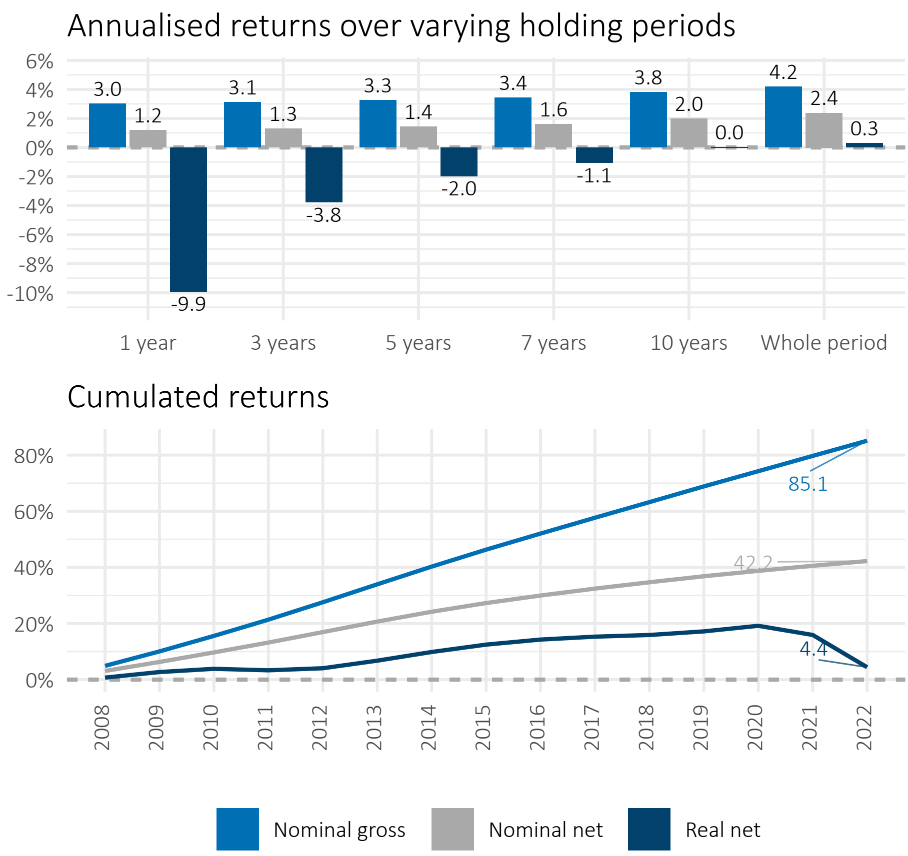
(-6.5%) for PIP unit-linked.

Returns in comparison

Overall, Italians are poorly served by their complementary pension saving vehicles. As Figure IT.11 shows, only two of the four analysed product categories offer a positive long-term real net return (over 15 and 23 years), and even then, both are below 0.5%.

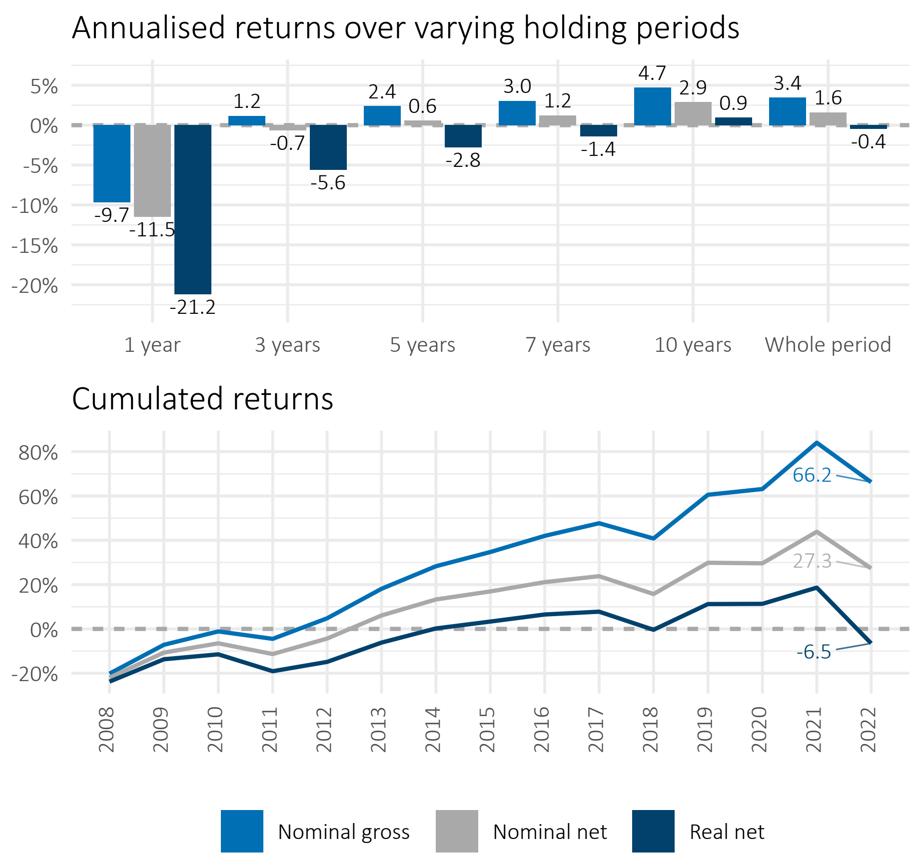
The cumulated real net performances displayed in Figure IT.12 tell the same story: after 23 years for pension funds and 15 years for PIP, Italian savers have at best marginally increased the real value of their pension savings.

Figure IT.9 – Returns of Italian PIP with profits (before tax, % of AuM)



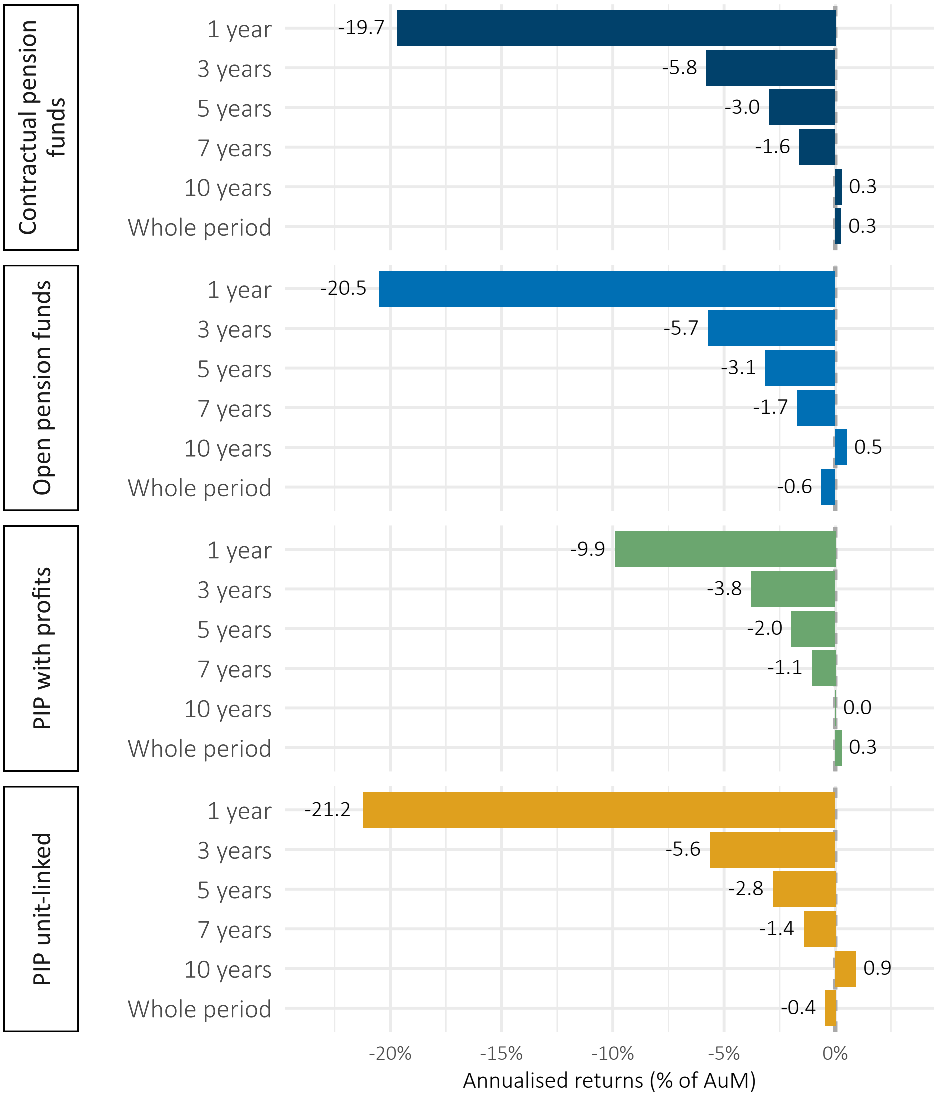
Data: COVIP, Eurostat; *Calculations:* BETTER FINANCE.

Figure IT.10 – Returns of Italian PIP with (before tax, % of AuM)



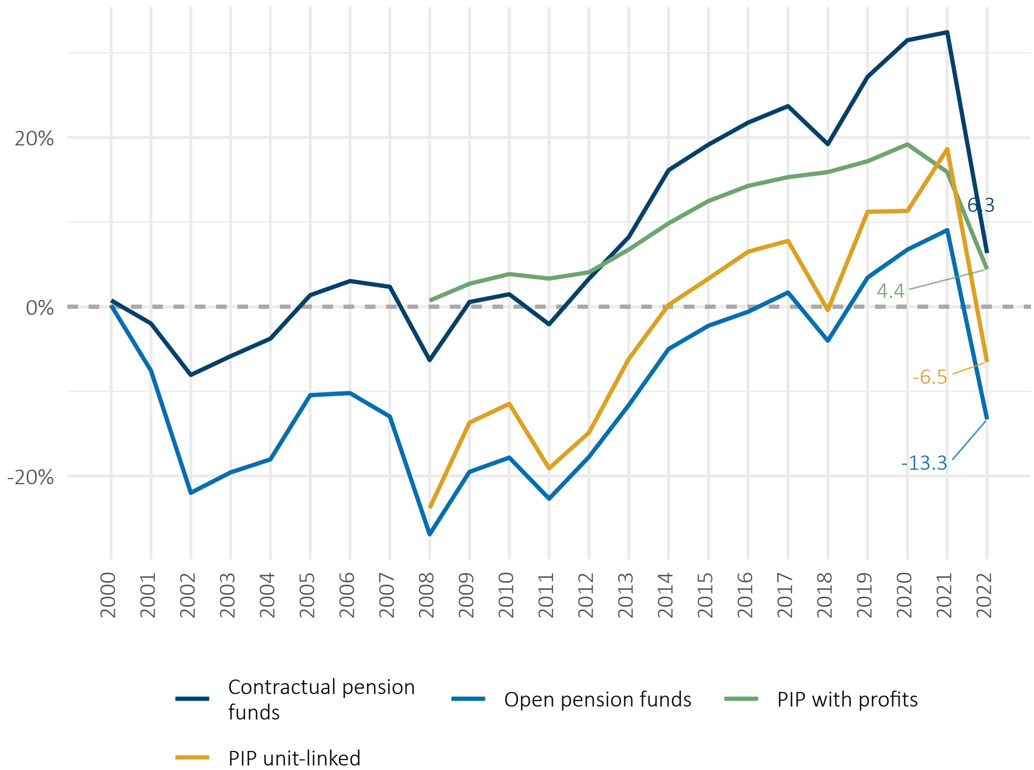
Data: COVIP, Eurostat; *Calculations:* BETTER FINANCE.

Figure IT.11 – Annualised returns of Italian long-term and pension vehicles over varying holding periods (before tax, % of AuM)



Data: COVIP, Eurostat; *Calculations:* BETTER FINANCE.

Figure IT.12 – Cumulated returns of Italian long-term and pension savings vehicles (2003–2022, before tax, % of AuM)



Data: COVIP, Eurostat; *Calculations:* BETTER FINANCE.

Do Italian savings products beat capital markets?

To compare the performance of Italian private pensions with that of European capital markets, we adapt the "default" benchmark portfolio presented in the introductory chapter of this report (Page 9). We keep the pan-European equity and bond indices as underlying values, but adapt the weight of equity in the mix in line with the average asset allocation of each product category. The parameters are summarised in Table IT.6

Table IT.6 – Capital market benchmarks to assess the performance of Italian pension vehicles

Product	Equity index	Bonds index	Allocation
Contractual pension funds	STOXX All Europe Total Market	Barclays Pan-European Aggregate Index	30.0%–70.0%
Open pension funds	STOXX All Europe Total Market	Barclays Pan-European Aggregate Index	30.0%–70.0%
PIP with profits	STOXX All Europe Total Market	Barclays Pan-European Aggregate Index	10.0%–90.0%
PIP unit-linked	STOXX All Europe Total Market	Barclays Pan-European Aggregate Index	65.0%–35.0%

Note: Benchmark porfolios are rebalanced annually.

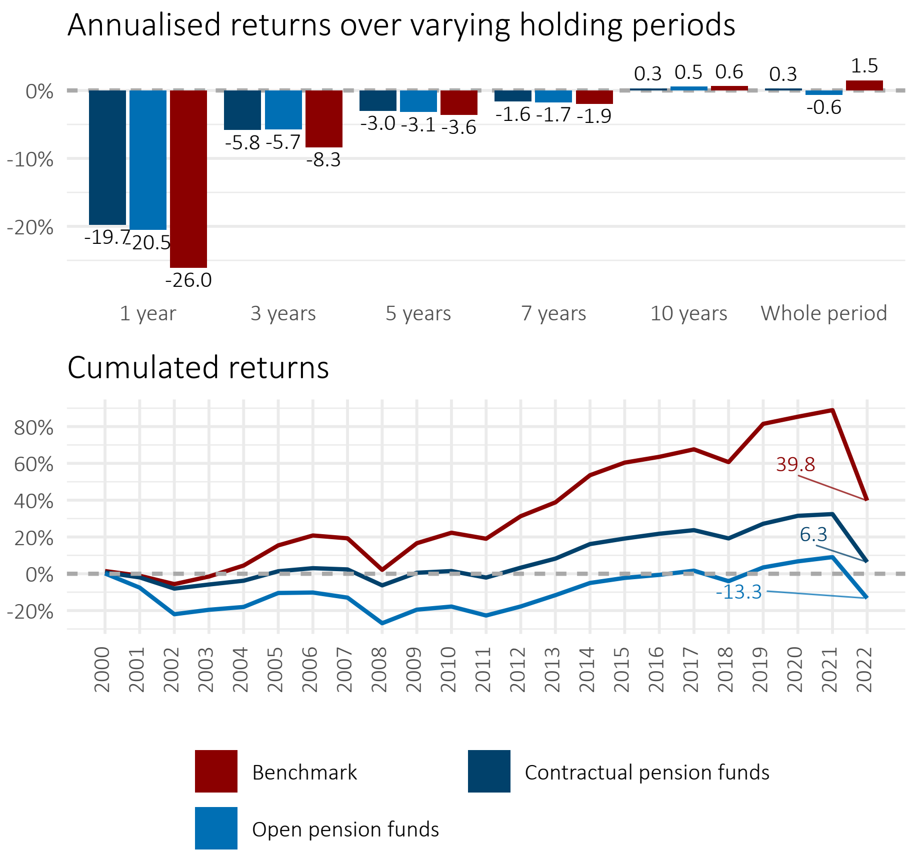
We calculate the real net returns of the benchmark portfolios based on these parameters. Annualised and cumulated returns are calculated since 2000 for occupational and open pension funds, since 2008 for "new" PIP.

As Figure IT.13 shows, neither contractual nor open pension funds manage to beat a 50% equity–50% bond benchmark. The annual average real return of the benchmark over 23 years is 1.2 pp superior to that of contractual pension funds, and 2.1 pp superior to that of open pension funds.

We use two different benchmark compositions to assess the performance of the two variants of "new" PIP in Figures IT.14 and IT.15. The sluggish though consistent return of PIP with profits do not enable it to beat the 10% equity–90% bond benchmark portfolio, despite the significantly worse performance of the benchmark in 2022.

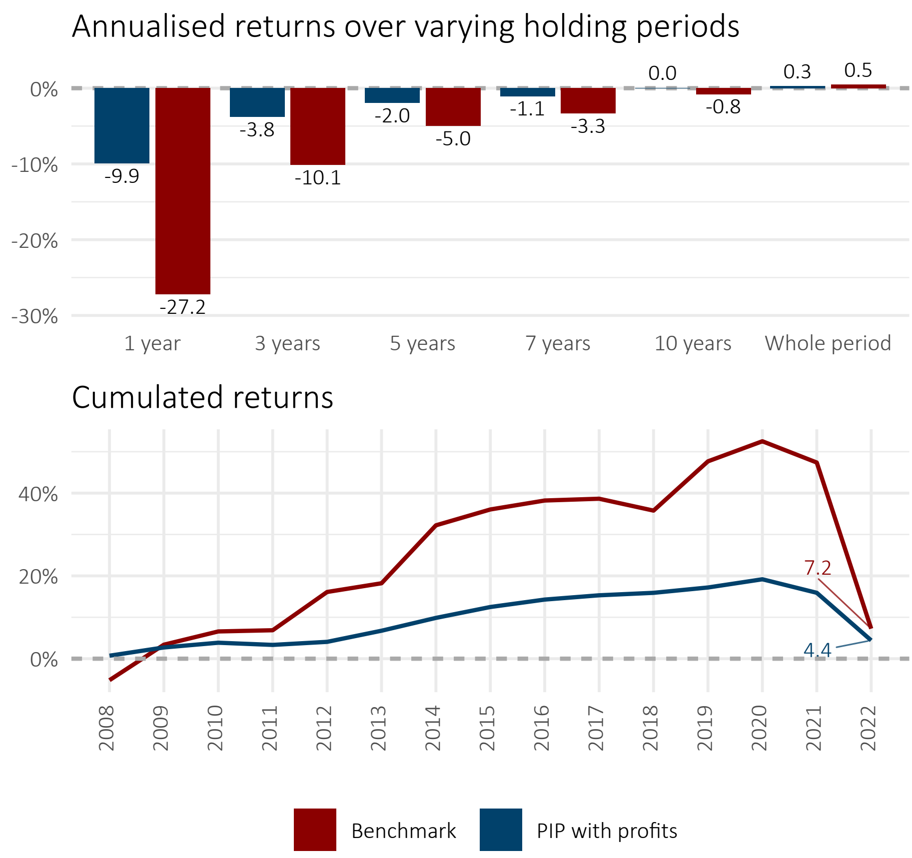
The comparison between PIP unit-linked and the 65% equity–35% benchmark is not flattering either for the former, that fails to beat the benchmark by 2.1 pp in annualised return over 23 years, and 36.1 pp cumulated.

Figure IT.13 – Performance of Italian contractual and open pension funds against a capital market benchmark (returns before tax, after inflation, % of AuM)



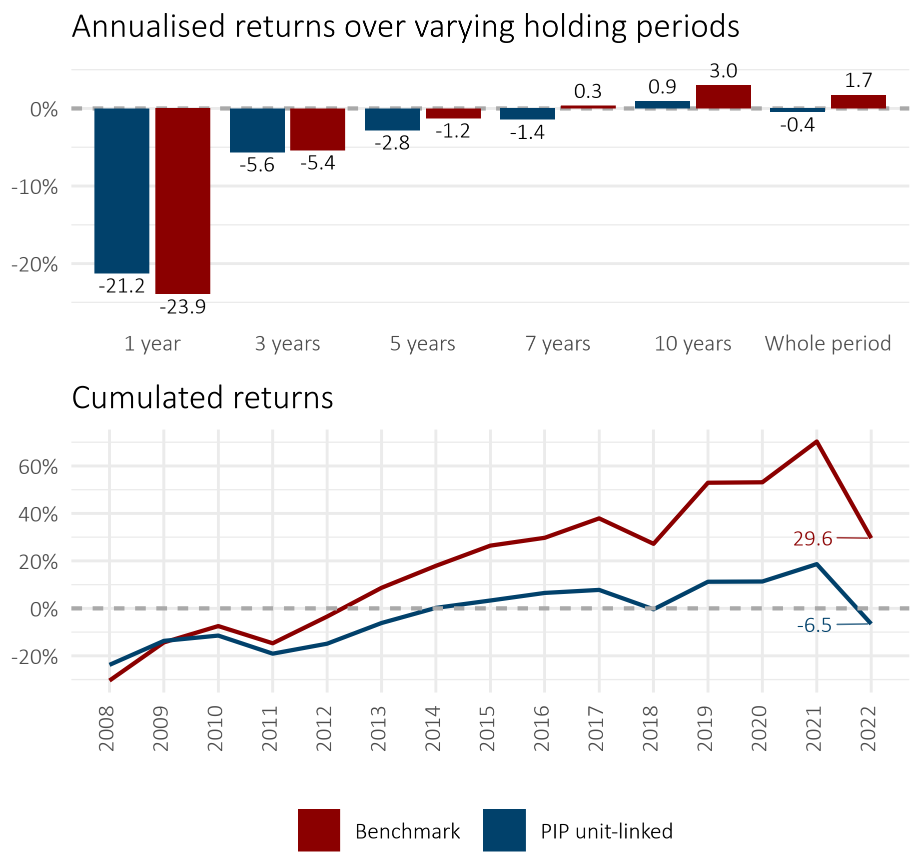
Data: COVIP, Eurostat; *Calculations:* BETTER FINANCE.

Figure IT.14 – Performance of Italian PIP with profits against a capital market benchmark (returns before tax, after inflation, % of AuM)



Data: COVIP, Eurostat; *Calculations:* BETTER FINANCE.

Figure IT.15 – Performance of Italian PIP unit-linked against a capital market benchmark (returns before tax, after inflation, % of AuM)



Data: COVIP, Eurostat; *Calculations:* BETTER FINANCE.

Conclusions

Italians still only rely to a limited extent on private complementary pensions. The State pension remains the major source of retirement income and both Pillar II and Pillar III cover a limited portion of the Italian labour force. The conservative asset allocation of occupational funds results in limited volatility, but also limits funds' ability to generate higher returns over the long term and significantly increase the purchasing power of Italian occupational pension savings. The high costs of open pension funds and, especially, "new" PIP eat close to half of the returns obtained on pension plan investments. Finally, in the long term, inflation is a major driver of underperformance: even before the 2021-2022 inflation rate hike, inflation had taken away the major part of the performance of pension funds and PIP performance.

Italian private pensions presents typical cases of insufficiently "aggressive" investment policies combined with high costs that make complementary pension funds—with the relative exception of contractual pension funds—unable to signficantly contribute to pension adequacy. In the context of an rapidly ageing population and high public debt and deficit that put an increasingly heavy pressure on the public pillar of Italian pensions, there is an urgent need to reorient investment policies towards higher risk but also higher yield markets by implementing life-cycle approaches that adapt risk-taking to the investment horizon of pension savers—in order to increase nominal gross returns—and a need to reduce costs, especially of "new" PIP. The upcoming reform of pensions, announced for 2024, should therefore go beyond public pensions and ensure that complementary pensions are effectively able to supplement the State pension.

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