A shift for long-term savings in Europe?

...article by Simon Colboc, FEPI Secretary General, as published in Dec. 2021 by www.fecif.eu

A recent study by CMI Strategies has revealed interesting trends about long-term savings in France and in Europe:

- There is a growing discrepancy in Europe between the need to increase long-term savings (not least for retirement) and the difficulty to find suitable investments.
- The need to save for retirement keeps increasing; at the same time there is a glut of additional savings following the COVID crisis, yet this extra money sits idle rather than being invested to produce long-term results.
- Governments are creating new long-term investment vehicles but are so far stopping short of actively recycling money earmarked for retirement but poorly allocated.
- Consumers are left to fend for themselves, with the wealthiest having access to professional advice and deploying their assets across innovative investment options from PE to infrastructure funds and ESG vehicles, while others are left out.

As is often the case, there is a lot of activity at both ends of the chain, inventing new tax wrappers and pushing investments, but very little attention paid to enabling consumers to take decisions that are right for them.

An increasing demand for long-term investing

CMI Strategies' investigations confirmed that there is considerable demand from consumers for long-term savings. Savings rates have been consistently high across Europe, and they have skyrocketed following the recent COVID-19 crisis. This crisis has generated 'forced' savings for entire categories of the population who were able to maintain their income but reduced their expenses as lockdowns greatly reduced opportunities to dine out, socialise or travel.

In France for instance, there was a staggering €267bn saved by consumers as of end of September 2021, or over €150bn more than expected. These 'COVID savings' are sitting in current accounts, as households seem to ponder what to do with them. Some will probably find their way back into the economy as delayed consumer spending – deferred holidays abroad or additional spending on home improvements. Some will also be kept available as emergency cash, as recent events have shown is important. But a large proportion will have to find its way into additional long-term savings and investments.

Taking a wider perspective, the same mechanism seems to apply across all European markets, and only to highlight the need to realign the c.€30tn "4th Pillar" financial assets consumers hold for long-term purposes but mostly keep in safe, low-return investments.

Old solutions no longer work

Funnelling long-term savings into the 'real' economy has historically been the main mission of institutional investors, pension funds or life assurers. These investors provided safe or even guaranteed investment returns and annuities to participants and policyholders. Financial market volatility and increased transparency (not to mention the end of the monetary illusion afforded by high inflation rates) has put an end to this period.

Defined Benefit pensions and UK-style With-Profits life assurance disappeared (for the most part) over ten years ago from the range of available solutions available to individual investors. Now, Continental guaranteed life insurance policies (such as the French Contrats en Euros or Belgian Branch-21 policies) are coming to an end as well. Financial returns for such products (largely backed by long-duration government bonds) were buoyed from 1990 to

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2020 by gradually declining interest rates. But all things come to an end, and these low interest rates are now creating a problem for investors, as financial returns barely pay for the institutions' running costs, not to mention paying a return to consumers.

Consumers are desperately looking for a substitute to the risk-free returns that used to be provided by capital-guaranteed life insurance policies. The plain truth is that such risk-free returns were historically provided through 'monetary illusion' as high nominal rates of return allowed for hefty expense ratios while leaving net returns that still appeared positive, even though they often were lower than inflation. And more recently from capital returns on long-duration bonds, as discussed above.

New structures and investments provide interesting perspectives

We are facing a fascinating combination of changes along the savings & investments value chain. The structures, tax wrappers and products designed to house investments are shifting as needs evolve. Governments used to favour life insurance as a good way to attract consumer savings and channel them into their own spending via gilts and T-bonds. Easy access to cheap sources of capital from capital markets have changed the perceived needs of governments and central banks. And the focus is now on channelling long-term savings towards retirement with the launch of the PEPP at EU level or the PER in France (which has already attracted over €45bn).

Consumers looking to allocate their investments over the long run are increasingly looking for alternatives to guaranteed life insurance policies. Impact investing, and generally funds with a strong and clear ESG angle are very successful nowadays, not just because regulators promote them but because, as asset management firms have witnessed during the recent COVID crisis, individual investors have been much more patient with such investments, resisting the urge to sell at the worst time even in a rocky stock-market.

Faced with the volatility of financial markets and the demise of guaranteed products, consumers are increasingly turning to a combination of real estate (often via real estate-based investment products such as REITs in the UK or SCPIs in France), structured products and Private Equity. The latter is the success story of the 2010's, attracting a growing proportion of savings, starting at the very high end but now reaching mass affluent clients. The good news is that these combined trends do make a lot of capital available to finance the 'real economy'.

Helping clients to the decision that is right for them

In this increasingly complex environment, it is not surprising that financial advisors are attracting a lot of attention. In places like France, PE funds have invested strongly in the industry, accelerating a wave of market consolidation and vertical integration. Financial advisors are more and more important to enable consumers to take stock of their own situation, assess their needs and their preferences, and chart the course to a secure financial future that best fits their situation.

This will succeed and generate profitable growth for all involved if it is done with a strong focus on serving the interest of consumers above all other considerations.

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