

Long term retail investment products

1. Current trends and best practices in the EU retail investment market

The Chair explained that although more young investors have entered the market recently, the level of retail investment in the EU remains lower than in the UK or the US. EU household investments in market instruments are worth around 100% of GDP, compared to almost 150% in the UK and 300% in the US. There are also strong differences between EU countries, but the strong results of some member states, such as Sweden and Denmark, demonstrate that improvement is possible.

A regulator stated that the diversity of national situations complicates the efforts to increase retail investment participation across the EU. The percentage of total financial assets held in bank deposits ranges from 20% in Denmark to 80% in Greece. The differences in national tax regimes and pension frameworks also incentivise different investment behaviours, with a focus on sovereign debt in Eastern Europe and Italy, pension funds in the Netherlands and life insurance products in France for example. While the landscape is diverse, one common EU wide issue is the excessive proportion of household savings being held in low yielding savings accounts instead of invested in the capital markets.

A second regulator described the current retail investment landscape in France. The financial wealth of French households is concentrated in low risk liquid products such as deposits and euro denominated life insurance. This conservative behaviour is partly explained by the high proportion of wealth held in real estate, which amounts to around 85% of median household wealth and results in limited capital market participation. Younger investors seem more willing to engage with financial markets, particularly via digital channels, which is positive. They also tend to invest in a more autonomous way than the rest of the population.

A third regulator explained that Denmark's retail investment success is grounded in long term structural commitments. The solution to driving more retail investment is to set the right framework conditions and allow participation to grow gradually. The Danish model, which is mainly based on the pension system, was developed through labour market agreements allowing the system to grow organically and sustainably, rather than through legislation and the creation of specific pension products. Initially modest contribution rates of around 5% to 6% of wages have grown to around 18% today. Trust has been central to this evolution. Employees have accepted lower wages in exchange for pension contributions in the future because they believed the money would be well managed and accessible upon retirement. Denmark's fully funded pension model, coupled with a prudent person principle that prioritises the long-term security of retirees, helped cement this trust. Auto-enrolment has also played a role.

An official observed that several other member states have successfully encouraged long term retail investment. The Netherlands have also successfully developed a strong pension system and Sweden's success is mainly founded on its ISK investment account.

2. The main challenges hindering long term retail investment

2.1 Structural challenges

The Chair emphasised that structural inefficiencies in the European investment landscape have resulted in higher product costs, which has had a negative impact on retail investors. The EU has over 35,000 UCITS funds, averaging \$0.4 billion in size, whereas the US has just 7,000 mutual funds averaging \$2.7 billion in size. This fragmentation increases costs, resulting in a 0.4% price premium compared to equivalent US products. Although this difference seems relatively small, it compounds over time.

An industry speaker challenged the idea that investment fund costs are a major issue in the European market, pointing out that active European UCITS funds are cheaper than their US equivalents. The use of asset-weighted cost figures disadvantages European funds due to their relatively small size, but the simple average cost of UCITS funds is in fact lower than that of US mutual funds: 1.04%, compared to 1.09% for US mutual funds. Additionally, prices for active UCITS equity funds have fallen by 6% over the last five years, despite high inflation. Furthermore, the European asset management landscape is highly competitive. There is strong product innovation and intense competition, with even the largest firms holding modest market shares. The issue limiting the development of retail investment is not the products themselves, but the environment in which they are used, which needs improvement. The underdevelopment of private pensions limits the level of long-term investment in the EU. A lack of awareness about long-term investment issues and limited financial literacy are further issues.

An official agreed that the structure of EU pension systems contributes to the under development of the capital markets. While 401(k) pensions play a key role in the US, most EU pension systems rely more on Pillar 1 state pensions, with Pillar 2 and 3 occupational and private pensions playing a relatively limited role, except in certain member states.

2.2 Financial literacy and behavioural challenges

A regulator stressed that weak investor engagement is correlated with the low level of EU financial literacy. There is also a strong degree of aversion to financial risk among a large part of the population, although the increasing number of people making potentially risky

investments in cryptocurrency shows that this picture is evolving.

An official agreed that the significant financial literacy gap of retail investors, even with respect to basic concepts such as compound interest, is hindering capital market investment. In addition, risk appetite, understanding and investment behaviour differ significantly by age group, socioeconomic background and also by country, due to cultural factors. In Ireland, for example, there is a long-standing preference for real estate despite past housing crises. Further assessment is also needed to understand the apparent contradiction between Europeans' risk aversion and the enthusiasm of many savers for investing in high risk cryptoassets.

An industry speaker concurred that the lack of awareness and financial culture in the EU is a major obstacle to long term investment. In France, for instance, young investors are predominantly investing in both ETFs and crypto, which hints at a degree of savings misallocation.

2.3 Tax incentives

A market expert noted that taxation also acts as a barrier to investment. In France, tax incentives favour liquid fixed income products in an excessive way. As a result, while Sweden's ISK covers 36% of the population, the French equivalent, the PEA, is only used by 10% of households.

An industry representative agreed that the lack of appropriate tax incentives is a major barrier. Incentives should focus more on long term investment in capital market instruments invested in specific geographies and sectors.

An official added that the persistent debt equity bias in most EU tax regimes for the issuance of securities must also be addressed, as it continues to hinder the development of corporate equity financing.

3. Policy objectives and approach for developing long term retail investment

3.1 Rationale for developing long term retail investment

A market expert highlighted the scale of the challenge facing long-term investment in Europe. To meet the needs of the green and digital transitions and stimulate sustainable growth, Europe must boost investment by up to €1 trillion per year. Given the limited capacity of public budgets and bank lending, a significant increase in equity and capital market financing is essential. While European households hold approximately €35 trillion in financial assets, the majority is concentrated in bank deposits and guaranteed products, rather than being channelled into long-term productive investments.

An official noted the potential challenge in reconciling the objective of encouraging retail investment in the capital market to achieve higher long-term returns, with the objective of channelling funds into the real economy. The Chair agreed with this comment, noting that

investors mostly seek to generate return on their investments rather than finance the economy, and therefore require diversification of their investments.

A regulator suggested that these two objectives could be reconciled by ensuring that policies and efforts to unlock retail savings to fund the European economy adopt an investor-centric approach that aligns with the long-term interests of savers. This approach must cover the entire investment journey, from initial contact to final investment decisions, and address the incentives and barriers that currently discourage retail participation.

Another regulator agreed that investor interests should be at the forefront of any policy actions. Europe's macroeconomic objectives are perfectly valid, but they are abstract concepts for investors. Investors must first be convinced of the merits of investing. Regulation should empower individuals to invest in their own best interests rather than channelling them into predefined product categories, particularly as digital tools enable more autonomous investment behaviour.

3.2 Proposed policy objectives and approach

A market expert suggested that stimulating long term investment in Europe requires a pragmatic, decentralised and iterative approach, rather than an additional EU level regulatory initiative. A coalition of willing member states and other actors should seek to develop common practices likely to foster long term investment. The Pan European Personal Pension Product (PEPP), which was an attempt to create a new European product has failed because it is too complex, trying to accommodate too many different stakeholder requests. Instead, Europe should build on the most effective national models, such as Sweden's ISK account or the Dutch and Danish pension systems and further develop them at European level. The same is true for tax incentives. Tax harmonisation is not a realistic objective, but member states could commit to ensuring that their national tax frameworks incentivise long term investment vehicles in a more consistent way.

A regulator agreed that it would be effective for the EU to take a bottom up approach, building on successful domestic products and tailoring them to national tax systems and cultural preferences. An official concurred that member states must learn from each other's experiences and capitalise on the existing products and best practices across the EU to adapt them across varying European market contexts. There are no easy fixes to the situation of retail investment, due to its cultural nature and the variety of tax incentives and market structures across Europe.

A second regulator acknowledged that the development of greater long term retail investment will require changes that go beyond the remit of EU policy, particularly in relation to national pension and tax systems. However, the EU regulatory framework should also be revisited to ensure that existing investor protection measures and distribution rules are not imposing excessive burdens. Retail investment products must also be simple, accessible and cost effective.

A third regulator welcomed the idea of exporting the Danish pension model to the rest of Europe. The two key factors contributing to the success of the Danish model

are trust and cost. Trust is particularly important for long-term investment products that use auto enrolment. Pension savers must be confident that their money will be managed in their best interests over many decades. Cost is also a highly important issue in the long term. Investors take on the risk and should not lose a large proportion of their returns to fees that are compounded over many years. Supervisors can play a key role in establishing benchmarks and encouraging providers to offer products at more competitive prices.

An industry speaker considered that fostering long term retail investment will require combining different solutions. Although there are many successful European examples to build on, variations in national circumstances and demographics make it difficult to define a unique solution. Different types of investment channels also need to be considered, such as direct digital channels, traditional advised channels, and indirect channels like insurance-based products and private pensions, as they all play different roles in attracting greater retail investment. Indirect channels, for example, can be more effective in encouraging novice investors to invest. Solutions must leverage these different channels and drivers.

Another industry representative agreed that developing the European capital markets will require the involvement of all financial providers and the leveraging of all available distribution channels and products.

4. Proposed policy actions

4.1 Strengthening the long term investment product offering at the EU level

Several speakers considered that the existing EU product frameworks are sufficient to support long term investment in the capital markets and that creating new product categories is not necessary.

An industry representative observed that the failure of the PEPP demonstrates the challenge of creating a single product for all European savers, given the diversity of market conditions and investor needs¹. A more effective strategy would be to ensure that the right incentives are in place to foster long term investment in existing products and adapting them, if needed, with targeted adjustments to align them with long term investment goals. Best practices across the EU, such as Germany's tax incentives and the Nordic pension models, should serve as guidance for this approach.

A second industry speaker agreed that existing product structures are broadly sufficient, although improvements are needed in the wider environment, particularly in terms of incentives and overall investor experience. Market conditions tend to have a more significant impact on long term investor engagement than the products.

A third industry speaker emphasised that UCITS funds are well suited for long term investment: they are simple, low cost and offer a wide variety of investment strategies. It is essential to preserve these characteristics and not re-open the UCITS Eligible Assets Directive.

A market expert suggested that given the diversity of market and tax situations across the EU, the most realistic product level measure to stimulate long term investment would be to establish a European label that promotes successful national products and ensures that best performing products are available in all member states. This label would apply to investment products that meet the following key principles: a long term investment horizon, no permanent capital guarantee, tax incentives for long-term investment and a focus on European assets. These products also need to be simple and easily accessible to retail investors. To support this approach, member states should ensure that labelled products are subject to the most favourable national tax treatment. An industry speaker agreed that a European label for long term investment products would be a constructive step forward. Such a label could support greater long-term investment in existing products such as UCITSs and ELTIFs without the need to develop entirely new products.

Finally, a regulator proposed the creation of a pan EU fund comparator, which would improve transparency and help investors make informed comparisons between the features, costs and returns of different funds.

4.2 Developing pension products and investment accounts

An industry speaker suggested that mechanisms such as pension auto enrolment and employee savings schemes can serve as effective gateways to capital markets.

Another industry speaker agreed that pensions are a more inclusive entry point than individual savings plans, which often require a higher level of financial literacy. Auto enrolment into workplace pension schemes is proven to build trust and promote inclusion in an effective way. While encouraging long term commitment is essential, investors must also retain the option to withdraw funds under certain conditions, as this flexibility supports long term engagement. Incorporating less liquid assets such as private equity and infrastructure into long term investment products is also important.

An official noted that Ireland is gradually introducing auto enrolment for pillar 2 occupational pensions, combining employee, employer and State contributions. As 30% of the workforce lacks a private pension, the primary aim of the reform is to improve retirement income adequacy, though it should also have positive spill over effects for the economy.

4.3 Improving financial education and tax incentives

A market expert emphasised the importance of improving financial education and fostering an equity

1. Several other issues with the PEPP were highlighted by the panellists. An industry speaker noted that the PEPP framework contains constraints related to double taxation, dual national compartments and a burdensome suitability process. Another industry speaker emphasised that the fee cap has contributed to the limited uptake of the PEPP.

culture across Europe. Such efforts must however leverage national specificities and best practices; in some countries, employer schemes are quite developed and may be effective in strengthening investor experience, while in others, different tools may be more suitable. Additionally, member states should commit to ensuring that national tax incentives target long-term investment vehicles and offer the most favourable tax treatment to labelled products.

An industry representative concurred that financial literacy plays an important role in incentivising long term investment. Beyond general education on basic financial concepts, savers need to understand the implications of the different types of products they can invest in. A second industry speaker added that a harmonisation of tax incentives would be beneficial. An official cautioned however that tax incentives should focus on optimising investor returns rather than prescribing the location or nature of investments.

4.4 Simplifying the investment process

A market expert stressed the importance of simplifying the investment process for retail investors. The current procedures for equity investment are cumbersome and much more complex than the procedures for investing in crypto. This complexity deters retail participation in the capital markets and must be addressed urgently. A regulator agreed that the investment journey must be streamlined for retail investors. Regulation should also support a more level playing field between traditional and crypto assets. A regulator added that due to MiFID and IDD requirements, advisors are increasingly reluctant to promote higher risk long term savings products.

An industry speaker agreed that overly complex compliance requirements and advice processes may discourage broader retail participation, especially in direct savings products. Another industry speaker concurred that the complexity of the investor journey is a potential obstacle to retail investment and hoped that this issue will be taken into account in the discussions around the proposed Retail Investment Strategy (RIS).

4.5 Leveraging technology

An industry speaker observed that technology has a key role to play in fostering retail investment. Technology can enhance transparency through better reporting, which allows investors to monitor their investments. The development of the appropriate technological infrastructure to do this will require effective public private partnerships.

An official noted that the regulatory framework should take account of the latest trends in digitalisation. Some digital developments can have ambivalent effects, however. While real time dashboards enhance transparency and empower investors, they can promote short termism by drawing attention to market volatility. There is also a general need for simplification of the regulatory framework.

A regulator observed that digital distribution channels can increase efficiency and reduce costs indirectly via competitive pressure in a more effective way than regulation alone. To remain relevant, regulation must adapt to evolving distribution models and digital trends. Distribution rules should reflect the growing trend of investor autonomy with the development of digital channels, which suggests that a new balance between empowerment and protection is needed. The emergence of cryptoassets must also be taken into account, ensuring a level playing field between cryptoassets and traditional securities.

5. Wrap up

The Chair summarised the discussion, highlighting the importance of considering long term investment from the perspective of the investor and focusing on simplicity, trust and new technologies. Employers can also play a pivotal role in encouraging investment participation. While the impact of costs is debateable, it is vital to ensure value for money. These changes will require long term effort. The Danish pension system, for example, was set up 60 years ago. There was a consensus among the panellists that there is no need for any new European products; instead, the approach should be bottom up and country led and should build on existing best practices at member state level.