Keynote speech - Insurance & the EU Retail Investor Strategy

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Thank you for the invitation and for the organisation of the conference by IVASS on the topic of "towards a consumer centric insurance".

And more specifically on the session on "insurance and the European Commission proposal on retail investor protection rules."

Insurers and their distributors play an important part in EU capital markets, both as investors of underlying assets and as providers of insurance based investment products to retail investors.

IBIPs and pension products represent about a third of EU household's financial assets, although there is a great variation across Member States.

About a third of IBIPs are unit linked products and the remining profit participation and hybrid.

Hence there can be no doubt that the insurance industry plays and will continue to play a crucial role in developing EU capital markets.

How the Commission is seeking to encourage retail investment

The Retail Investment Strategy

On 24 May of this year the Commission adopted a proposal for an ambitious package of measures that we know as "the Retail Investment Strategy".

With this proposal, we are putting in place another key building block of the Capital Markets Union.

Our starting point is to put the retail investor at the centre of our policies and to boost consumer trust.

We believe that the most effective approach to enhancing participation is to put in place a framework in which retail investors feel empowered and adequately protected, and confident enough to reap the opportunities that investing in Europe's capital markets can provide, so that they are better able to cater for their short and long-term financing needs.

And more retail investment in our capital markets is good for our prosperity, because those savings can be put to use efficiently and reinvested into businesses, to the benefit of the broader European economy.

An important cornerstone of the strategy is that the retail investors should be able to use the capital markets in order to build up long term savings, to meet their retirement needs.

That should in particular entail facilitating investment in products that are suitable for long term investment strategies.

The problem with retail investment in Europe…

At the moment, regrettably, retail investor participation in the EU is low – too low when compared with international standards and worrying when we look towards the longer term.

Just 17% of EU household assets are held in financial securities, compared to 43% in the US.

Too many EU consumers demonstrate poor understanding of the investment environment: levels of financial literacy in the EU are also very low – if many citizens are unable to understand the basic principles of finance and financial products, that is an important factor limiting the growth of the retail investment market.

Faced with lack of knowledge and a fundamental asymmetry of information, retail investors have become heavily reliant on the advice they receive from intermediaries.

However, the evidence also points to low trust levels that retail investors have in their advisors: 45% of Europeans are not confident that the investment advice they receive is actually in their best interest.

At the same time, investment products available to retail investors tend to be expensive. Certain products on the market, especially more complex structured products, carry high costs that eat into net returns.

It is therefore hardly surprising that many EU citizens with capital to invest choose to put their money elsewhere, into other projects for example, simply leaving it in the bank on deposit accounts - to get eaten up by high inflation.

It is only by addressing these issues that we can increase retail investors' trust in the markets and persuade them to invest more so that they can constitute an adequate capital base to cover their retirement needs.

How the Strategy seeks to address the problems…

Our strategy contains a range of enhanced protections along the length of the retail investor journey.

The measures proposed are ambitious and broad as they cover all distribution channels and investment products including all PRIIPS as well as financial instruments.

This way we can ensure level playing field in the level of investor protection.

They have been designed to address, in a targeted way the shortcomings we have identified.

They include:

- improved disclosure and marketing rules ensuring transparency and adapting the framework to the digital age.
- enhanced financial literacy,
- improved suitability and appropriateness assessments,
- raised professional standards for advisors,
- strengthened rules on inducements,
- strengthened rules on product governance to ensure value for money;

- strengthened supervisory enforcements rules, and
- easier access to products and services for sophisticated investors.

Let me touch on the first four topics more specifically:

1. Disclosures and Marketing

We have proposed targeted changes to improve transparency for retail investors, including transparency of cost disclosures, while at the same time modernising disclosure rules so that they are fit for the digital age.

The strategy also introduces specific measures to strengthen rules around marketing communications.

Because as the digital world is rapidly changing, it brings new types of marketing activity. Our package strengthens investor protection by making clear to firms what their obligations are with regard to marketing communications. It also equips supervisors with tools to better enforce the rules.

Our aim is to ensure that marketing communications are clear, fair, not misleading, regardless of the channel through which they are distributed and irrespective of whether communicated directly by investment firms or indirectly, for example via financial influencers or “finfluencers”. It is particularly important to ensure the rules are effective and protect younger generations of investors, who tend to be more tech-savvy but may be less experienced and more exposed to risky investments pushed by misleading marketing campaigns.

2. Financial literacy

Increasing the levels of financial literacy is one of the Commission’s priorities under the 2020 Capital Markets Union Action Plan. As I mentioned, the levels of financial literacy in the EU are very low, as confirmed in the dedicated 2023 Eurobarometer survey: only 18% of EU citizens have a high level of financial literacy, 64% - a medium level, and the remaining 18% - a low level. If it is our aim to help more people invest, raising levels of financial literacy is a crucial component of the broader set of measures.

For those consumers that struggle to understand financial matters, transparency rules designed to highlight important aspects of a financial service offer are unlikely to be of any great help. Increasing complexity and sophistication of financial products only underlines how important it is to promote financial literacy.

The Commission has been working on initiatives designed to improve financial literacy levels. Together with the OECD and Member States, we have developed a financial competence framework for adults to define crucial competences and now also one for youth. It will be particularly important to address younger investors, who typically have less financial knowledge and more risky financial behaviour. According to the October 2022 Flash Eurobarometer survey on retail financial products, young people were found to be less confident than older generations when managing their personal finances. At the same time, they tend to be more attracted by crypto-assets and place more trust in social media as a source of information.

The focus on youth is of particular importance when considering the longer term challenges. It is not just about competence – about knowing how to invest and in which products. It's about making sure that younger generations are able to recognise that they are likely to need a capital base in later life, and that the best way to constitute that base is to begin investing sufficiently early with a considered long-term strategy.

3. Inducements

On the topic of inducements, the impact assessment identified shortcomings in the way investment products are designed and distributed, linked to the potential conflicts of interest arising from the payment of inducements by product manufacturers to distributors.

The Commission stepped back from proposing a full inducement ban and instead opted for a staged approach, introducing a set of restrictions and safeguards in relation to inducements and advice.

We have proposed a partial ban for execution-only sales of products (without advice) because even where no advice is provided, the payment of inducements can still lead to higher costs for retail investors and more prominent promotion of induced products.

When advice is provided, we have also proposed tougher rules to ensure that firms act in their clients' best interest. The new "best interest test" replaces the existing quality enhancement and no detriment tests and sets concrete criteria to be followed to ensure that advisors to act in the best interest of the client.

The Commission intends to monitor how the situation develops: we will take another look and evaluate the situation three years after adoption.

4. Value for Money

Reports from ESMA and EIOPA indicate that some products sold to retail investors provide little, if any, value to the retail client, in particular due to high costs of products. EIOPA and ESMA have been working to address these issues.

The Value for Money assessment in our proposal is not fully new, but builds on and enhances existing product governance requirements. The aim is to ensure that products that do not provide Value for Money are not put on the market.

Under the new rules, manufacturers and distributors will need to assess cost and performance and to compare their product against a relevant benchmark (of similar products), if available, developed by ESMA or EIOPA.

The intention is to identify outliers and ensure that those products which do not provide value are not put on the market and sold to retail investors.

I would like to stress that the Value for Money concept does not look at cost alone, but that cost is assessed in view of the characteristics, objectives, the strategy of the financial instrument and its performance.

Conclusion

There are many other measures that I have briefly mentioned before that make the Retail Investment Strategy a complete, ambitious, retail investor-focused package. It has been designed to address the identified shortcomings, and in particular to remedy the deficit in consumer trust that is evident from the recent surveys.

By strengthening the investor protection framework, providing citizens with the means, the knowledge and the confidence to invest in capital markets, we can help them to help themselves provide for their future needs.

The strategy is currently under negotiation in both the Parliament and the Council, and many stakeholders have commented on our proposal – often from very different perspectives.

And some progress has already been made.

The Council has had 5 negotiation sessions (working parties) where all issues have been discussed in a first round.

We expect a report from the European Parliament where they define their position at the beginning of next year.

The most controversial issues are – as we had expected – the parts on how to deal with conflict of interest (including a partial ban on inducements) and the issue of value for money. The co-legislators will have the final say on these key issues. It will probably be difficult to finalise these negotiations under the current Commission mandate. So we have a few more months of heated debates and discussions ahead of us!

I believe, in any case, that we all share the overarching goal to increase retail investor participation. To achieve that, we need to be ambitious. This is a fight for the benefit of future generations – and we cannot afford to lose. I count on your support to push for an ambitious outcome that brings meaningful change.

Thank you for your attention!