Investment asset amounts, allocation and returns at the end of the second quarter of 2014

Investment portfolio nearly 170 billion euros

During the second quarter, the investment portfolio of earnings-related pension insurers increased by EUR 3.7 billion, to EUR 169.2 billion. The increase during the first six months of the year totalled seven billion euros.

The share of fixed-income investments fell, equities rose and real estate remained steady.

At the end of June 2014, the investment portfolio of the whole sector was allocated roughly as follows: investments in equities and equity-like instruments, 47.1 per cent (EUR 79.7 billion); fixed-income investments, 42.5 per cent (EUR 72.0 billion); and real estate investments, 10.4 per cent (EUR 17.5 billion).

During the second quarter, the share of fixed-income investments fell (-1.4 percentage points), while the share of equities and equity-like instruments rose (+1.4 percentage points). Real estate investments remained steady. The changes in percentage points that occurred at this rough level of allocation during the second quarter were greater and opposite in direction when compared to the first quarter of this year with its cautious start. The joint effect of the two quarters was as follows: the share of equities and equity-like instruments increased (+0.7 percentage points, EUR +4.5 billion); the share of fixed-income investments shrank (-0.6 percentage points, EUR +2.0 billion), as did the share of real estate investments (-0.1 percentage points, EUR +0.5 billion).

A replay of the first quarter: bonds increased and loan portfolios shrank

The trend that had characterized the first quarter continued during the second quarter for bonds and loan portfolios. The value of bonds rose by EUR 3.9 billion during the first half of the year. New purchases exceeding maturities and sales totalled EUR 1.7 billion. The rest was attributable to market trends. Since interest levels have been falling during the current year, the prices of interest-bearing papers and the market values of fixed-income investments have risen. This trend has been stronger for corporate bonds than for government bonds.

As in previous years, investment loans and TyEL relending continue to decline. The total sum of these two types of loans fell by EUR 0.6 billion, to EUR 4.8 billion, during the first half of the year. TyEL relending accounted for the bulk of this shift. The loan portfolios had last been at this level before the financial crisis set in, i.e. before 2008. New investment loans and TyEL relending granted by pension insurance companies during the first half of the year reached the relatively high figure of EUR 0.75 billion. Most of these loans were granted to group companies; less than EUR 0.2 billion was granted to enterprises outside the own group. It still seems that there are no major problems in the availability of financing for Finnish enterprises. Financing can be obtained on competitive terms from sources other than pension insurers.

Changes from the previous quarter: **money market investments decreased, listed shares and hedge funds increased**

During the second quarter, money market investments decreased by EUR 2.1 billion. Although this investment category increased during the first quarter, the category on the whole declined by EUR 1.2 billion during the first six months of the year. It seems that uncertainty about the direction of the financial markets boosted money market investments during the first quarter. On the other hand, it also seems that during the first quarter, assets were left waiting in money market instruments that were easy to convert into cash, until they were invested in longer-term instruments during the second quarter. Within the past few years, money market investments have accounted for about 5–8 per cent of all investments. At the end of June 2014, the figure was 5.1 per cent.

During the second quarter, investments in equities and equity-like instruments increased by a total of EUR 4.0 billion, of which EUR 2.3 billion came from the rise in hedge fund investments and EUR 1.7 billion came from the rise in listed shares (including funds). New hedge fund investments outweighed sales by EUR 2.0 billion. The remaining EUR 0.3 billion of the increase in this investment category was due to a positive market trend. The sales of listed shares (including funds) outweighed purchases by about EUR 0.4 billion. Despite the sales, the volume of this investment category increased as the result of a positive stock market trend. A typical share index in an industrialized country rose by 2–5 per cent during the second quarter.

In the same way as last year, the purchase and sales data on equities and equity-like instruments indicate a continuing trend where investments in equities other than listed ones seem to be favoured. During the first quarter of 2014, new investments focused on other equities, i.e. private equity and unlisted shares. In contrast, the second quarter of 2014 resumed the trend of 2013, when purchases focused more on hedge fund investments. This trend can be ascribed, on the one hand, to the investment environment, in which it is difficult to achieve returns on fixed-income investments and, on the other hand, to the need to improve the diversification of the portfolio and to reduce the portfolio’s dependence on the development of listed equities.

The trend of the past few years continued: investments outside the eurozone on the rise

A shift of -2.3 percentage points from domestic investments to investments in the rest of the eurozone (+0.4 percentage points) and outside the eurozone (+1.9 percentage points) was recorded during the second quarter of 2014. At the end of June, domestic investments totalled EUR 46.7 billion (27.6 per cent), which is EUR 2.8 billion less than at the end of March. At the end of June, investments outside the eurozone totalled EUR 79.8 billion, or 47.2 per cent of all investments. The remaining investments focused on the eurozone (excluding Finland), totalling EUR 42.7 billion, or 25.2 per cent.

The most important changes in domestic investments arose when assets invested in money markets were transferred elsewhere (EUR -1.4 billion) and listed shares were sold (EUR -0.7 billion). Although, in the short term, domestic investments have been replaced by investments in other countries, the euro amount of domestic investments has increased year by year for the past decade. The figure of EUR 30.2 billion at the end of 2004 had risen to EUR 49.5 billion at the end of 2013. Apart from the size of the sum invested in Finland, it is worth noting that the investments in Finland exceed the sum invested in the rest of the eurozone in total.

New purchases of government bonds in excess of sales and maturities accounted for EUR 1.0 billion of the increase in the eurozone (excluding Finland). The rest of the increase (EUR +0.6 billion) was the consequence of a positive stock market trend. The rise in investments outside the eurozone consisted of new purchases exceeding sales: hedge funds (EUR +2.0 billion) and listed shares (including funds) (EUR +2.4 billion).

The return trend improved as the year advanced

In terms of returns, the earnings-related pension insurers have had a positive start for 2014. The second quarter was slightly stronger than the first. For the whole sector, the nominal return during the first six months came to 4.4 per cent.

The current year has been marked by uncertainties; for instance, the situations in Ukraine and the Middle East and the blurred prospects for economic growth the world over. Despite this, the year has so far offered investors fairly good opportunities for profitable investments. The return trend on the North American stock market has been better than that on the European stock market. A clear difference exists between the two continents as concerns economic growth and its expected future trend. This difference is also reflected in the ways that the central banks have tuned their monetary policies. In the USA, the Federal Reserve has continued to reduce bond purchases, and now in late summer there has even been talk about potential times for raising interest rates. In contrast, the European Central Bank further eased its monetary policy in June. So far, the current year has been better for fixed-income investments than the year 2013. Especially when geopolitical uncertainties have raised their head, fixed-income investments have attracted more interest. The weak outlook for economic growth in Europe and the ECB's monetary policy have supported the European government bond market, where interest rates have fallen to levels that are clearly lower than at the start of the year. Shifts on the American government bond market have been much more moderate. Corporate bonds have shown a much better trend than government bonds.

Thanks to the positive equity market trend, pension insurers achieved their best category-specific return rates from investments in equities: 6.5 per cent. Alongside the falling interest rates, the prices of interest-bearing papers have risen, especially for corporate bonds. So far, the year has also been fairly good for fixed-income investments: +3.1 per cent. Moreover, the returns on real-estate investments continued their typically good trend that kept up with inflation: +2.7 per cent.

The total returns for the various groups of earnings-related pension providers (public-sector pension providers, pension insurance companies, company pension funds and industry-wide pension funds) fall within a narrow range, from 4.1 to 4.8 per cent. Requirements for solvency have only been laid down for private-sector pension providers.

The return trend has also continued to be good when seen over the long term. The average annual real return for the entire sector from the beginning of 1997 to the end of June 2014 is 4.1 per cent. The corresponding return rate in the private sector is 4.0 per cent and for the public-sector pension providers 4.4 per cent. The Finnish Centre for Pensions uses 3.5 per cent as the assumption of real return in its long-term projection.