Amounts and allocation of investment assets at the end of September 2015 and returns in January–September

1. The investment portfolio continued to decrease during the third quarter of the year

At the end of September 2015, the total amount of assets put into funds by earnings-related pension insurers, i.e. the investment portfolio, came to EUR 176.0 billion. In the third quarter, the investment portfolio decreased by EUR 6.9 billion, when compared against the second quarter. Assets had also decreased in the second quarter – albeit more moderately – by about EUR 1.3 billion, when compared against the first quarter. On the other hand, assets had increased by as much as EUR 11.7 billion in the first quarter. In consequence, for the period between the start of 2015 and the end of September, the investment portfolio increased by EUR 3.5 billion. Private-sector pension insurers' assets declined by EUR 4.0 billion in the third quarter, while public-sector pension insurers' assets decreased slightly less in absolute terms, or by EUR 2.9 billion. These changes in the portfolio figures within nine months did not alter the relative shares between the public-sector and private-sector pension institution groups.

One reason for the diminishing investment portfolio in the third quarter was the negative return trend. However, it should be noted that the low-key return trend was not the only reason for the decrease in assets. Another noteworthy reason is that, at the same time, the pensions paid out from the assets exceeded the pension contributions collected into the system. In fact, assets are put into funds and invested so that some of the financing needed for pensions can be obtained from these sources.

Both in 2014 and during the first three quarters of 2015, the returns on pension investments exceeded the financing needed for pensions from investments. Some of the returns have been left in funds, where they are invested and used to cover the increased pension liability.

2. Fixed-income investments rose, equities down and real estate steady

At the end of September 2015, the investment portfolio for the whole sector was distributed between the main categories as follows: investments in equities and equity-like instruments, [1]47.2 per cent (EUR 83.1 billion); fixed-income investments, [2]43.4 per cent (EUR 76.3 billion); and real estate investments, 9.4 per cent (EUR 16.6 billion).

The euro amounts of the various investment categories developed uniformly during the third quarter, when compared against the second quarter. In the third quarter of the year, the share of equities and equity-like instruments shrank by 0.7 percentage points (EUR -4.5 billion), whereas the share of fixed-income investments rose by 0.7 percentage points, despite the decline in their value in euros (EUR -1.7 billion). Real estate investments had a negative change in euros (EUR -0.5 billion) but their relative share remained steady as the whole investment portfolio declined.

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[1]When the analysis refers to investments in equities and equity-like instruments, this means the following categories of investment figures: listed shares (incl. funds); hedge funds; and other investments in equities, which include, for instance, equity investments and investments in unlisted shares.
[2]When the analysis refers to fixed-income investments, this means the following categories of investment figures: money market investments; investment loans; TyEL relending; and bonds.

The combined effect of the three quarters of the current year, when seen against the situation at the end of 2014, was as follows: the share of equities and equity-like instruments shrank (-1.7 percentage points, EUR -1.3 billion), as did the share of real estate investments (-0.5 percentage points, EUR -0.5 billion), while the share of fixed-income investments increased (+2.2 percentage points, EUR +5.3 billion).

2.1 Money market investments, bonds and convertible bond portfolios shrank

At the end of September, the investment portfolio of bonds and convertible bonds came to EUR 60.3 billion while money market investments totalled 11.7, investment loans 2.9 and TyEL relending 1.4 billion euros. Changes in the third quarter were opposite to those in the second quarter, especially with regard to money market investments. The net decrease of EUR 1.7 billion in fixed-income investments between the third and the second quarter was attributable to a decline in the value of money market investments (EUR -0.8 billion) and bonds and convertible bonds (EUR -0.9 billion). In contrast, the amounts of investment loans and TyEL relending remained unchanged. The fastest growth among the various types of fixed-income investments between 1 January and 30 September was recorded for money market investments (EUR +4.1 billion), followed by bonds and convertible bonds (EUR +1.4 billion).

The decline of bonds and convertible bonds in the third quarter was solely the result of negative value changes. When interest rates – or investors' return requirements – rise, the prices of interest-bearing papers fall. This means that the market values of interest investors' portfolios decline. It should still be noted, however, that the net flow of bonds was positive for about EUR 0.6 billion. This, in part, offset the shrinking of the bond portfolio. A positive net flow is obtained when the purchases of an investment instrument exceed its sales and maturities. Correspondingly, the net flow is negative when sales and maturities exceed purchases. The decrease in the money market investment portfolio stemmed from both negative value changes (EUR -0.5 billion) and a negative net flow (EUR -0.3 billion).

New investment loans and TyEL relending granted by pension insurance companies totalled about EUR 0.17 billion during the third quarter of the current year. The overall situation after three quarters is that the value of new investment loans and TyEL relending granted totals EUR 0.53 billion. However, this figure is not as high as it was at the same time the year before, when the value of new investment loans and TyEL relending totalled EUR 0.95 billion. These figures give an indication of the availability of financing for Finnish companies from sources other than earnings-related pension providers. The higher the figures for these two types of loans are, the more challenging it is for companies to obtain financing from other sources. During the financial crisis and soon thereafter, new investment loans and TyEL relending totalled clearly more, about EUR 0.4–3.0 billion per quarter. At the end of September, the portfolio of investment loans and TyEL relending totalled EUR 4.3 billion.

2.2 A clearly negative change in value for listed shares

The net decrease in investments in equities and equity-like instruments (EUR -4.5 billion) was attributable to the unfavourable value change trend. Negative changes in value totalled approximately EUR -5.5 billion. In part, the decrease in the portfolio of equities and equity-like instruments was offset by the positive net flow of investments, which came to about one billion euros. Since this investment category increased by EUR 5.8 billion in the first quarter, fell by EUR

2.6 billion in the second quarter and further by EUR 4.5 billion in the third quarter, the total change during the first three quarters of the year was minus EUR 1.3 billion.

As a whole, the net flows of investments in equities and equity-like instruments were negative by about EUR 4.6 billion during the first three quarters. Especially in the first quarter the net flow was clearly negative, as sales exceeded purchases by about five billion euros. Selling slowed down clearly during the second quarter and a shift to purchases was evident in the third quarter. One factor explaining the eagerness to buy may be the rapidly falling share prices; in other words, pension insurers have found suitable stock to buy on the falling markets. On the other hand, the exceptionally low interest rates on bond markets also have an impact on the current trend; in consequence, it is now challenging to hunt for returns on bonds. It is therefore fairly natural that the search for returns shifts to other investment instruments, such as – in part – equities and other equity-like instruments.

In summary it can be concluded that the third quarter of the current year was not good for the value changes of equities and equity-like instruments, especially when compared against the first quarter. Owing to the weak third quarter, the return on listed shares among TELA's five largest private-sector pension insurers, for instance, has been only about 1.1 per cent when calculated from the start of the year. Returns were much greater during the first six months of the year, when they reached about 12 per cent. The euro-denominated index values for returns on listed shares in various industrialised countries (including the world index) reflect the sluggish global trend on the stock markets. The return indices increased by 2.3–3.3 per cent during the first three quarters: MSCI Europe Index 3.3%, OMXH Portfolio Index 3.1% and MSCI World Index 2.3%.

3. The increase in the share of investments outside the euro area came to a halt this year

During the third quarter of 2015, the share of investments outside the euro area declined slightly when compared against the second quarter (-0.1 percentage points, share 50.0 per cent). Finland's share also diminished (-0.2 percentage points, 27.3 per cent). In contrast, the share of investments in other euro area countries (excluding Finland) rose (about 0.3 percentage points, 22.7 per cent). During the first three quarters of the year, the share of both Finland and countries outside the euro area has risen by exactly one percentage point, while the share of other euro area countries has shrunk by two percentage points. It is worth noting that investments in countries outside the euro area have had a rising trend for roughly the last ten years, but this year the share seems to have levelled off at about 50 per cent.

4. A clearly slower trend for returns as the year advanced

The returns of the seven largest earnings-related pension insurers during the first three quarters of 2015 ranged from 1.1 to 3.1 per cent. For comparison's sake, after the first two quarters the corresponding figures were still between 3.7 and 6.6 per cent. The average total return for the investments of these earnings-related pension insurers was 1.9 per cent after the first three quarters. Similarly, the mean return for the investments of the five largest private-sector pension insurers, calculated from the start of the year to the end of September, was 2.1 per cent, while the mean return for the two largest public-sector pension insurers was 1.7 per cent.

Among the investment categories, equity investments accounted for the best mean return percentages. Real estate investment funds also yielded good returns. In contrast, the returns on listed shares and fixed-income investments were weak.

The average annual nominal return for the entire sector from the beginning of 1997 to the end of September 2015 is 5.8 per cent. The corresponding real return is 4.1 per cent. The nominal return rate for the private sector is 5.7 per cent and for the public-sector pension providers 6.1 per cent. The real returns are 4.0 and 4.4 per cent, respectively. The Finnish Centre for Pensions uses 3.5 per cent as the assumption for real return in its long-term projection. When making comparisons, it is good to remember that requirements for solvency have only been laid down for private-sector pension providers.

5. Uncertainty of the markets in the third quarter

In terms of returns, the third quarter of the current year was poor, especially for listed shares, throughout the world. However, the year started very positively for returns. This was mainly due to the announcement of the European Central Bank (ECB) that it would launch an expanded asset purchase programme with the aim of accelerating economic growth and inflation in the euro area. However, the mood shifted after mid-June, when the downturn on the Chinese stock market and the slow progress of loan negotiations with Greece caused uncertainty on the markets. Uncertainty increased even more in the third quarter, when concern over slower economic growth in China and the impacts that shrinking growth would have on the world economy as a whole spread across markets. In addition, the intentions of the Federal Reserve (Fed) to tighten monetary policy, and the associated market expectations, caused restlessness on the financial markets as well as capital drains from the developing economies, owing to increased pressures for strengthening the dollar.

However, the last quarter of the year started on a positive note: the stock markets have partly recovered from the fall that took place in August–September; the central banks, such as the ECB, Fed and the Central Bank of China, have continued their stimulating monetary policy; and U.S. businesses have released positive reports concerning their financial performance in the third quarter. In contrast, the financial figures of European and Japanese companies have fallen below expectations. Nevertheless, positive development of the real economy is possible, especially in the euro area, thanks to lower oil prices, the weakened euro, and the ECB's lenient monetary policy. On the other hand, the risks affecting the real economy and markets, such as concerns over China's economic growth and the financial problems of other developing economies, should not be belittled. The only thing that is certain is that the values of investment portfolios will continue to fluctuate on the financial markets.

Earnings-related pension providers in the private sector must meet the statutory solvency requirements. The solvency of pension providers was strong at the end of September. This is one element in their preparations for potential uncertainties on the financial market. The solvency ratios of the five largest pension insurance companies ranged between 14.5 and 30.6 per cent at the end of September.