



PIR light and shadow

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How the introduction of long-term saving plans impacted the Italian SMEs capital markets. What shall we expect from recent regulatory changes?

In 2017, following the example of the French Plans d'épargne and the UK's Individual Saving Accounts, Italy encouraged its asset managers to create long-term saving instruments called Piano Individuale di Risparmio (individual savings plan or PIRs). PIR benefits from tax incentives to encourage savers to invest in small and medium-sized firms. [➤](#)

| | PIR Piani Individuali di Risparmio | PEA-PME Plan d'épargne en action— Petites et Moyennes Entreprises | ISA Individual Saving Account |
|-------------------------------|--|--|---|
| Country | Italy | France | UK |
| Date of inception | 2017 | 2014 | 1999 |
| Maximum investment (per year) | €30,000 | - | £20,000 |
| Maximum investment | €150,000 | €150,000 | - |
| Holding period | Five years | Five years | - |

Essentially, the PIR is a mere "tax container" that will assume different technical forms such as UCITS, segregated accounts, insurance contracts, deposits of financial assets. Within these long-term saving plans, savers can place any type of financial instrument (shares, bonds, UCITS shares, and derivative contracts) or sum of money, while respecting certain investment constraints, with the benefit of an exemption from 26 percent income tax and inheritance taxes if savers hold their investments for at least five years.

The purpose of PIRs is to stimulate the growth of Italian enterprises and therefore the Italian economy, with a focus on a specific category of enterprises (i.e. Italian SMEs). In order to be PIR-compliant, there are some specific constraints that an investment plan must respect:

- Specifically, at least 70 percent of invested assets will consist of Italian companies
- 30 percent of the mentioned share must be directed to SMEs not included in the FTSE MIB index (equal to a minimum percentage of 21 percent of total investments)

Additionally, some limitations on the amount invested in PIRs and regarding counterparty concentration risks apply:

- It is not allowed to invest more than €30,000 per year (and more than €150,000 per investor over five years)
- It is prohibited to invest more than 10 percent in instruments from the same issuer, in order to ensure portfolio diversification

The PIR-compliant financial products shall be issued by companies residing in Italy, EU or EEA, with the exception of the "free" portion of the investment that may also include instruments issued by companies from "non-white list" countries.

An opportunity for support of SMEs growth: strengths and weaknesses of PIRs

After the 2008 financial crisis, Italian financial markets suffered from a major loss of confidence towards investment funds by private investors. Therefore, in order to support the direction of individuals' savings towards Italian companies, some specific economic policies were adopted by the Italian Government. In 2014, the PIR-compliant form of saving was introduced with the objective of facilitating long-term investments in Italian SMEs, and acting as a catalyst for the real economy.

The introduction of PIRs, fulfilling both social security needs and liquidity management purposes from an investor's perspective, has been particularly innovative. It underpins a flow of financial resources from private savers to Italian SMEs, which have historically experienced difficulties in achieving emancipation from the bank lending channel.

One important aspect to be highlighted is the level of diversification. A PIR allows the asset manager to craft a highly diversified portfolio and to considerably reduce the overall risk of the investment, making it an attractive solution for investors with different degrees of risk aversion. Nevertheless, it is clear that it has been designed for retail investors, unable to autonomously diversify the portfolio without incurring high costs, rather than for professional players.

When going through the main strengths of PIR, it is necessary to start off with duration. The Law states a minimum holding period of at least five years and, due to a further inheritance tax exemption, it results in a mid to long-term investment horizon. As a matter of fact, this instrument is characterized by lower flexibility when compared to traditional saving plans ("Piani d'Accumulo") and pension funds.

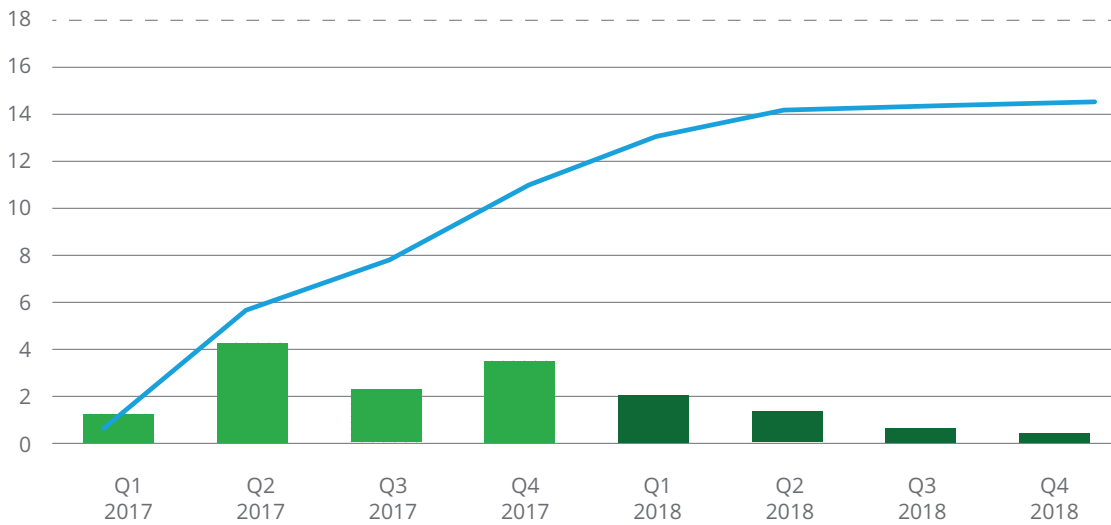


The overall impact on private investors has been positive. It has allowed them to channel a considerable and unexpected amount of resources towards domestic SMEs, help reduce their strong dependence on the banking system, and provided support to their IPOs.

2018. The great success in 2017 was slowed down by the negative market trend in 2018. In our opinion, the reduction in net sales only confirms that Italians investment decisions are strongly influenced by market trends. Asset managers and distributors confirm that investors' interest in PIR-compliant funds remains unchanged. ➔

The table shows the trend of PIR-compliant mutual fund net sales during 2017 and

Net Sales 2017 - 2018
In €Billion



Source: Assogestioni (Italian association of Asset Managers)

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Aside from these desirable attributes, it is also crucial to take into account some potentially detrimental aspects.

In the first place, the distribution of investments between different asset classes may not be appropriately balanced because most of the SMEs operate in a very complex and volatile environment. Moreover, since eligible instruments in the portfolios will be issued by Italian companies, an inherent country risk might be hardly diversified away.

Last but not least, some potential drawbacks are connected to the quality and reliability of the information available about shares issued by SMEs considering their nature and relative size, and given the difficulties in retrieving historical data related to their performance.

Asset management industry in Italy, investors and PIRs

Over the past twenty years, the Italian asset management industry has experienced considerable renovation due to changes in legislation. During the 1980s in particular, an increase in the demand for a new form of investment took place, due

to the fact that Italy was living in a period of welfare growth. Therefore, collective investment funds were introduced to the Italian market, offering the opportunity to private investors to benefit from professional low-cost strategies in order to increase their financial income. Around the 2000s, a consistent growth in the market's dimension was observed. Asset under management (AuM) in particular saw an increase from €880 to 1,131 billion in just four years (2003-2007). In the same period, the products offered to investors shifted to more diversified solutions.

However, when the financial crisis reached Italy in 2008, the outflow of resources managed by investment funds caused by the loss in value of their financial products, resulted in a total reduction of around

€200 billion in AuM (causing an overall slump to €84 billion).

On the basis of this unforeseen experience, regulation became even stricter to ensure once again the transparency and to prevent other "black-swan" events. The Italian — and the greater European — financial regulators tightened the rules concerning rating agencies, hedge funds, and OTC markets.

Nowadays, investment managers and asset managers in Italy are offering a more international and modern approach to investment products. This has suited investors who are looking for less volatile and risky solutions, rather than those offered by the Italian financial markets before the financial turmoil.

On the other hand, the financial resources "crunch", together with a restrictive fiscal stance, has weakened Italian SMEs and their ability to access capital.

In this context, the introduction of PIRs, mainly leveraging on the fiscal deduction and covering the gap between international and Italian financial existing tools, has been favorably welcomed by the markets.

In order to fully understand the positive effects of PIR on the Italian market, it is important to look at the profile of a typical Italian investor. In a nutshell, they are on average not sophisticated investors (lack in financial education is an issue that has been highlighted also by the Regulator), they are considerably risk averse, and continue to prefer the traditional banking channel.

A net overall fundraising of almost €68 billion from PIR introduction is expected by the end of the fifth year against an initial forecast of €18 billion.

Nevertheless, in the last two years, the share of people with positive saving rates has boosted from 43 to 47 percent. This figure is supported by the widespread increase in financial knowledge and the expansion in terms of number of investors within the overall population.

Furthermore, it is worth remembering that fiscal incentives are highly appreciated by investors considering the Italian hyper-taxed system.

The results surpassed expectations. The net sales of PIR-compliant products in the first year of their launch outperformed the annual target (€1.8billion), reaching an unforeseeable figure of €10.9billion in 2017.

This was particularly significant with respect to the €18billion of targeted collection originally expected by Italian regulators during a five-year period. It has been observed that AuM for 2018's year-end almost reached €17.4billion.

The means by which different asset managers have embraced the change and developed distinct ways of offering their PIR-compliant products can be broadly divided into three clusters:

- Institution of a new fund/product compliant to the PIR regulations
- Transformation of an existing fund/product into a PIR-compliant one
- A mixed approach combining new and existing funds

During 2018, the positive trend was confirmed with over 50 new PIR-compliant funds created.

After two years, the strong demand for PIR was not sustained by an increase of new investment opportunities in SMEs, which has exhibited soaring prices of their stocks though. For further context, before the introduction of PIR, the average Price to Earning was 12.4, while at the end of 2018

it had reached a ratio of 17.6, showing that resources invested were not matched by a sufficient variety of investment opportunities.

At the end of 2018, analysts confirmed the favorable trend showed no sign of slowing in the forthcoming years. A net overall fundraising of almost €68billion from PIR introduction is expected by the end of the fifth year against an initial forecast of €18billion. ➔





The empirical evidence

Deloitte has promoted a study, carried out jointly with Jeme Bocconi and the law firm NCTM, aiming to understand the real impact of the PIRs introduction on Italian markets in terms of volume of transactions.

As mentioned, PIR's portfolios must be composed of at least 21 percent of instruments issued by SMEs, generally listed on AIM Italia market or included in either FTSE Italia SMALL Cap or FTSE Italia MID Cap indexes.

Applying a statistical mean-test among daily volumes of shares traded in 2016 and 2017 in the AIM market, there emerged a remarkable increase of 338 percent. It has been quite straightforward to assess a correlation between the flow of financial resources to the market connected with the PIR investments and the augmented average number of trades observed.

With respect to the SMALL and MID indices, the effect was slightly smaller in magnitude, but still statistically significant. The positive change drove the yearly average traded

volumes up by +39.6 percent and +35.0 percent respectively.

Furthermore, comparing the growth in volumes in Italy and France (where, as mentioned, a similar financial tool has been introduced in recent times) a significant correlation was noted between the French SME market (PEA) and the Italian one.

In a similar fashion, the number of subscribers also grew unexpectedly. Italians investing in PIRs were around 700,000 by the end of 2018 and half of them had subscribed to a fund for the very first time.

Thanks in part to the PIR, the total number of Italians owning investment fund units has grown to 12 percent of the entire population, with half of them holding more than €14,400 stakes. The main asset classes held are flexible funds (36.4 percent), bond funds (28.1 percent), balanced funds (10.9 percent) and equity (6.9 percent).

Despite the remarkable changes in market volume, it must be stressed that this was partially due to the initial dimensions of the domestic SME market that were considerably small. Nevertheless, the great impact on the overall transactions is clearly the aftermath of the investment funds' entrance in the market.

During 2017, SMEs' shares prices were growing, on average, more than the market index. Furthermore, during the bearish trend of 2018 prices of SMEs stocks were decreasing consistently less than the broad market index. Nevertheless, no abnormal trends have been observed to presage a bubble effect.

Conclusion

The 2019 Italian Budget Law introduced new additional constraints, attracting much criticism from the sector's operators. For PIRs constituted from 1 January 2019 onward, it is stipulated that at least 3.5 percent of their underlying assets should be invested in small and medium-sized entities listed on unregulated markets (i.e. AIM/MAC) and a further 3.5 percent in venture capital funds.

The review of the standard was intended to expand the contribution that PIRs can give to the real economy and, in particular, to SMEs and start-ups.

Even if the intentions of the legislator are embraceable and praiseworthy, the drawbacks linked to these additional constraints appeared immediately clear to the operators. Both the AIM/MAC and the venture capital markets in Italy do not present the size and characteristics necessary to absorb the demand for investments that would presumably come from the PIRs.

Moreover, and most importantly, the new rules would oblige the PIR-compliant products to hold a minimum 7 percent of their portfolio in illiquid instruments (a figure approaching the maximum limit set by Bank of Italy, being equal to 10 percent). This "immobilized" component could represent an issue for open-end funds, which must guarantee the units are redeemable and which typically calculate their NAV on a daily basis.

The asset management industry and its stakeholders were hoping for a step backwards by the regulators. This potential regulatory misstep has meant

an interruption in the launch of new plans. In practice, savers who had started to feed a plan before 1 January 2019, were able to continue to do so on the basis of previous standards, while asset managers had put on hold the commercialization of new products, pending clarification of the new rules.

The implementation decree has been published in early May, confirming the new constraints included in the Budget Law. The Economic Development Department declared that the effects of the implementation Decree will be monitored in order to evaluate remedial actions.

Many market participants wonder whether the open-end funds may constitute the optimal PIR-compliant structure in light of the new standards, as opposed to closed-end financial products. In this regard, it is worth noting that the legislator is exploring fiscal incentive measures in favor of European Long Term Incentive Fund (i.e. ELTIF) subscribers.

In conclusion, the new legislation has so far inhibited the spread of a product that was giving fruitful results, actually achieving the economic policy objectives

that were originally set. Financing SMEs and diminishing their dependence on the traditional banking channels, are indeed fundamental aspects to ensure the competitiveness of the Italian economic system. The widespread sentiment in the industry is that the new constraints could represent the final blow to a successful and farsighted initiative and leading, ultimately, to a total eclipse of PIRs. ●



To the point:

- PIR collections higher than expected, in particular in the first year (2017)
- Empirical analysis showing a significant impact on SMEs capital markets
- New constraints included in 2019 Budget Law: an attempt to amplify the impact on SMEs induced by PIR that could conversely bring to the final eclipse of the instrument