

Eurosif's Response to the European Commission Consultation: Undertakings for Collective Investment in Transferable Securities (UCITS) - Product Rules, Liquidity Management, Depositary, Money Market Funds, Long-term Investments

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Eurosif¹, the European Sustainable Investment Forum, welcomes this Consultation on the UCITS framework. This response focuses on the more conceptual section on how to foster a culture of long-term investment in Europe.

Eurosif is supportive of the renewed attention on long-term investing as a mechanism for generating sustainable growth in Europe. It is promising that regulators and legislators have acknowledged that a shift in the balance of capital allocation away from short-term to long-term is needed in order to restore confidence in the financial industry.

Before considering the specific questions posed by the Commission in the Consultation paper, Eurosif would make the following points:

- Many of the characteristics of long-term investments described in the Consultation document are correct: projects with long time horizons, infrastructure financing, stable returns that are less correlated with the market. However, low level of liquidity and long lock-up periods are not unique characteristics of long-term investments. Many long-term investments can be liquid, and many short-term investments can (as seen in the financial crisis) become illiquid. Liquidity is a characteristic of the market, not the investment time horizon. A good definition of long-term is provided by the World Economic Forum (WEF): *"Long-term investing can be usefully defined as investing with the expectation of holding an asset for an indefinite period of time by an investor with the capability to do so. Investors engaged in long-term investing are less concerned about interim changes in asset prices, and instead are focused on long-term income growth and/or long-term capital appreciation both in their initial evaluation and continued interaction with their investments."*²
- The risk/return profile of long-term investments is particularly sensitive to environmental, social and governance (ESG) concerns.³ Institutional investors are becoming more interested in long-term holdings such as infrastructure

¹ Interest Representative Register ID number: 70659452143-78

² Source: World Economic Forum (2011), The Future of Long-term investing.

³ See for example: DB Climate Change Advisors (2012), Sustainable Investing: Establishing Long-Term Value and Performance.



investments, and it will be critical for the success of these projects that ESG concerns are addressed over the lifetime of the project.⁴

This response has been developed as a part of Eurosif's aims to develop sustainability through European financial markets. It does not necessarily reflect the views of all its Members and Member Affiliates.

Question 1

What options do retail investors currently have when wishing to invest in long-term assets? Do retail investors have an appetite for long-term investments? Do fund managers have an appetite for developing funds that enable retail investors to make long-term investments?

The first point that Eurosif would like to make is about the definition of long-term and what it relates to. The concept of what long-term investments are does not seem to be clearly defined, or is defined in our view with a very narrow perspective. Long-term investments can be illiquid, but they do not have to be. Long-term investments can be certain asset classes such as infrastructure, private equity or real estate, but they can also be fixed income or public listed equity.

Eurosif strongly recommends that, if long-term investments are to be subject to a separate legal framework, then the definition of long-term investments itself must be thoroughly considered, for example through a separate consultation.

We would argue that other types of investments can (or should maybe) incorporate a long-term perspective and that this should not be forgotten in the drive to generate the change needed to reorient the markets to a more long-term perspective. This is especially important when one considers that investments not mentioned by the Commission constitute the bulk of the market for investments. This is also emphasised in the WEF report: "*Long-term investing has not proved easy to define as it more closely resembles an attitude towards investing than an investing style that can be captured in a single formulaic sentence.*"

Concerning the retail market and bearing in mind the well-documented growing public pension gap, retail savers/investors will be looking for sustainable investment solutions that can deliver viable financial returns over multi-decade horizons (typically 20 to 30 years or more).

However, selecting and incorporating such investments into the portfolio of a retail investor requires a high level of care. Certain products have characteristics that make them interesting channels for retail investments, including pension savings, long-term employee savings plans, occupational pension funds and life insurance products.

⁴ See inter alia Eurosif's report on the Infrastructure sector and the European SRI Study 2012, both available on the Eurosif website.



As always, transparency, clarity and education is needed in order for the retail market to appropriately incorporate such investments into their portfolios. Trust is still an issue in financial sector, and as noted in a recent survey by EFAMA, communication, better advice and more understanding of investors' needs is required to restore trust.⁵

When looking at appetite for long-term investing, it is also useful to draw a parallel to the market for sustainable and responsible investments (SRI), as SRI investors tend to be more long-term in their investment decision making. Eurosif's recent European SRI Study 2012⁶ shows a growing appetite for and sophistication of investors in terms of incorporating ESG concerns. However, this growth is primarily found in the institutional market, while the retail market, on aggregate is not growing as fast.

Question 2

Do you see a need to create a common framework dedicated to long-term investments for retail investors? Would targeted modifications of UCITS rules or a stand-alone initiative be more appropriate?

Yes, we see a need for a common framework to ensure appropriate protection for investors, for the investees and for the economy at large.

However, different appropriate approaches could be combined:

- Targeted modifications of the UCITS rules should avoid splitting the framework, as this could cause confusion and undermine the success of the UCITS brand. Instead, one can modify the framework to allow a certain allocation to long-term investments within the framework;
- In combination with this, a bespoke framework for more pure long-term investment funds or specific assets can be developed. This framework can provide a platform for raising awareness of long-term investments and deepening consumer education.

Within these frameworks, long-term products should also be required to incorporate ESG concerns, since these have a long-term effect on portfolio risk and return. As these investments also have a societal benefit though supporting sustainable growth, it would be appropriate to consider promoting the use of such products for example through incentives.

Question 3

Do you agree with the above list of possible eligible assets? What other type of asset should be included? Please provide definitions and characteristics for each type of asset.

Eurosif does not agree with restricting the definition of long-term investing to the assets described by the Commission in the Consultation paper.

The definition of long-term asset should incorporate projects with a long completion time horizon, such as infrastructure. However, the Commission must also include other asset

⁵ See: <http://www.efama.org/Pages/Long-Term-Savings-EFAMA-Survey.aspx>

⁶ Available: <http://www.eurosif.org/research/eurosif-sri-study/sri-study-2012>

types that are not necessarily restrained by liquidity, but are often invested in for an indefinite time horizon. It is dangerous and counterproductive for the Commission to restrict the definition, as it necessarily implies that all other assets are short-term. Therefore, the definition should be extended to equity and fixed income funds under specific conditions, e.g. where they incorporate ESG concerns.

Question 4

Should a secondary market for the assets be ensured? Should minimum liquidity constraints be introduced? Please give details.

See response regarding eligible assets. This question is only relevant for specific assets or products, and is too specific in a conceptual section on how to foster a culture of long-term investments in Europe.

Question 5

What proportion of a fund's portfolio do you think should be dedicated to such assets? What would be the possible impacts?

If the proposed narrow definition of long-term investing is referred to, then funds should have the freedom to be specialist fund managers with 100% of the portfolio in long-term investments. It would be up to each investor and their advisors (whether qualified or non-qualified) to ensure an appropriate portfolio balance and whether the product is suitable to the investors' objectives. However, when incorporating other forms of investments and recognising that long-term is an attitude more than a liquidity profile, the discussion of the proportion of fund portfolio allocated to such investments must be framed in the context of the definition used.

Beyond that, one can reasonably argue that long-term retail products such as supplementary pension's savings should incorporate a certain amount of long-term assets. The French *fonds solidaire* may serve as such a model.

Question 6

What kind of diversification rules might be needed to avoid excessive concentration risks and ensure adequate liquidity? Please give indicative figures with possible impacts.

See response regarding eligible assets. This question is only relevant for specific assets or products, and is too specific in a conceptual section on how to foster a culture of long-term investments in Europe.

Question 7

Should the use of leverage or financial derivative instruments be banned? If not, what specific constraints on their use might be considered?

(8) Should a minimum lock-up period or other restrictions on exits be allowed? How might such measures be practically implemented?

See response regarding eligible assets. This question is only relevant for specific assets or products, and is too specific in a conceptual section on how to foster a culture of long-term investments in Europe.

Question 8

Should a minimum lock-up period or other restrictions on exits be allowed? How might such measures be practically implemented?

See response regarding eligible assets. This question is only relevant for specific assets or products, and is too specific in a conceptual section on how to foster a culture of long-term investments in Europe.

Question 9

To ensure high standards of investor protection, should parts of the UCITS framework be used, e.g. management company rules or depositary requirements? What other parts of the UCITS framework are deemed necessary?

Yes. Part of the success of the UCITS framework is its high level of transparency and investor protection. This should be continued in any new framework for long-term investments. Eurosif believes that transparency for investors is critical, and has developed the European Transparency Code⁷ for funds to support its mission in promoting transparency on ESG considerations.

Question 10

Regarding social investments only, would you support the possibility for UCITS funds to invest in units of EuSEF? If so, under what conditions and limits?

Yes. Please see Eurosif's position paper⁸ on the EuSEF framework for more detail.

⁷ See: <http://www.eurosif.org/sri-resources/sri-transparency-code>

⁸ See: http://eurosif.org/images/stories/Eurosif_Position_Paper_-_EC_Social_Business_Initiative.pdf



About Eurosif

EUROSIF, the European Sustainable Investment Forum, is the pan-European network whose mission is to develop sustainability through European financial markets. Eurosif works as a partnership of the national Sustainable Investment Forums (SIFs) within the EU and with the support and involvement of Member Affiliates. Recognised as the premier European forum for sustainable investment, Eurosif's Member Affiliates are drawn from leading institutional investors, asset managers, NGO's, trade unions, academic institutes and research providers, together representing assets totalling over €1 trillion. Eurosif's work includes a focus across asset classes - equity and fixed income markets, microfinance, renewable energy, property, private equity and hedge funds - all centred on the industry trends and future legislation affecting this space. The key benefits that Eurosif Affiliate Members receive include EU interfacing, SRI information and European wide initiatives that integrate Environmental, Social and Governance (ESG) issues into the financial services sector.

For the full list of Eurosif Member Affiliates, please see www.eurosif.org

Eurosif has two main roles: (1) to provide an international forum that allows members and member affiliates to work together on issues pertaining to Sustainable & Responsible Investment (SRI, see below for definition of SRI and its market size in Europe) and Corporate Governance in the EU financial services sector, and (2) to collect input from members and member affiliates and then communicate their ideas and initiatives to European policy makers, including the European Commission as well as the European Parliament. Therefore, this note is mainly driven from and by the interest and expertise of our membership.

Sustainable and Responsible Investment Definition

Eurosif continues to use the term SRI as the most readily acknowledged expression for this field and defines SRI as follows:

Sustainable and Responsible Investing (SRI) is a generic term covering any type of investment process that combines investors' financial objectives with their concerns about Environmental, Social and Governance (ESG) issues.

Market Size

Eurosif published Sustainable and Responsible Investment (SRI) figures and trends in its European SRI Study 2012. This unique study highlights the scale of European SRI as well as European and National trends across fourteen countries. The Study is available for download on the Eurosif website.