PRESS RELEASE

THE "SURVEY ON ITALIAN SAVINGS AND FINANCIAL CHOICES 2016" PRESENTED TODAY IN TURIN BY INTESA SANPAOLO AND THE EINAUDI CENTRE

- **For Italian households, the recovery is slow but the outlook is improving.**
- **Investors save to cope with uncertainty, but the proportion of savings put towards retirement remains small.**
- **With zero rates, real estate and cash deposits polarise investments.**

Turin, 21 July 2016 – The "Survey on **Italian Savings and Financial Choices 2016** - Low Rates and Volatility, a Return to Real Estate" was presented today in Turin. The study was carried out by the Einaudi Centre and Intesa Sanpaolo on the basis of interviews conducted by Doxa in January and February 2016 of 1,011 households with bank and/or postal accounts. In each household, the main decision-maker on saving and investment issues, i.e. the person best informed about and most interested in the subjects raised in the questionnaire (in 77% of cases, the head of the household), was interviewed. The sample selected is representative by age group, profession, academic degree and geographical area. The study, which allows for the comparison of periods from 1983 to the present, **focuses on a single theme each year: in 2016 this was investment choices in conditions of low or zero rates.** An additional sample set was created through 312 interviews of a target of small investors aged 29 to 55. The interviewees in the additional sample were then combined with those in the "household" sample belonging to the same target (255), for a total of 567 heads of household: these were surveyed concerning their reactions to the "zero rate" scenario and the attractiveness of real-estate investment. The results were analysed and discussed by **Salvatore Carrubba**, President of the Einaudi Centre, **Gregorio De Felice**, Chief Economist at Intesa Sanpaolo and the economist **Giuseppe Russo**, editor of the report. The conclusions were drawn up by **Gian Maria Gros-Pietro**, chairman of Intesa Sanpaolo.

The following is a summary of the research :

- **Families: the recovery is slow, but the outlook is improving.** The crisis now appears behind us, but among families there is a widespread perception that the disposable income that was lost has never been fully recovered: as a result, spending in 2015 and 2016 remained subdued. However, it bears emphasising that the share of families in the sample who report insufficient income stabilised at around 17% in 2016, without declining, while expectations showed real improvement. Until 2015, 50% of interviewees viewed an imminent deterioration of their economic condition as probable. In 2016, the proportions are reversed: 60% believe that an improvement is imminent. What is more, in 2016 20-22% of the sample were considering not merely maintaining, but even increasing, spending on their children and stepping up expenditures on health and the purchase of durable goods, which they had put off in previous years.

- **Demographic development over the past decade stabilises savings at the level of 2012.** The economic crisis expedited the impact of population ageing on the distribution of the sample by working status: in eight years, the share of retirees in the sample increased by over 10 percentage points, with an equal reduction in both self-employed workers and employees. Considering that the ability to save declines as an investor ages, the demographic change has an adverse impact on savings. When the crisis began, the numerous baby boomer generation was in business, at the height of careers in which they had seen their incomes constantly increase. After seven years, the same generation began to leave the workplace, sometimes with smaller pensions than expected. In some cases, they lost their jobs without finding another equivalent position. The replacement generation, i.e., the cohorts that ought to have entered the workplace, had fewer opportunities. Consequently, in 2016 the incidence of investors in the sample stabilised (40%), whereas there was a slight reduction in the share of income saved (9.6%): in terms of the sample average, both percentages remained at the levels of 2012. The "economic landslide" of the middle class (i.e., the central portion of the income, savings and wealth distribution), highlighted by the 2015 Survey, is a structural phenomenon that influences the central part of all of the distributions, and thus affects the average speed of the recovery, the average share of investors and the amount of income allocated to savings, despite the improved structural conditions.

- **Investors save to cope with uncertainty. Savings for children still exceeds savings for homes. Pension expectations continue to decline, but too little is being saved for retirement.** The weak recovery, combined with financial market volatility and low returns, underlie the increasing "precautionary" motivation for savings (58.3%, up by 10 points). There was a slight increase (from 8% to 8.5%) in savings for homes, but savings for children (17.1%) continued to exceed savings for homes. The ratio of these two motivations was reversed before the crisis, when savings for homes exceeded savings for children.

- **Retirement savings are still insufficient.** The intention to save for old age is still quite low in comparison to potential needs (14.1%). This is the case even though there is a widespread, correct perception of the reduction of future pension benefits compared to those enjoyed by previous generations: the balance between the expectation of sufficient or insufficient income when entering retirement declined from 13% to 6.7% (29.8% before the crisis). Just 11% of the sample stated that they had contracted some form of supplementary pension, falling under pillar II or III of the pension system. The percentage is particularly low among those who have just begun to make retirement contributions.

- **Capital protection is always the priority.** Despite less concern that capital will be lost - indirectly indicated by the fact that the percentage of interviewees not interested in the economy (53.5%) once more exceeds that of those interested in it (46.5%) - when heads of household invest they report that their number-one priority is "security" that capital will not be lost (58.3% in 2016, 52% in 2015 and just 23.8% in 2011). Only then come return (15%), liquidity (14%) and long-term capital appreciation (7%).

- **Asset management is gaining ground, to the detriment of direct investment, on which decision-making is increasingly complicated.** The traditional investment through which Italians have protected their savings, while also earning solid returns, is represented by bonds, with government bonds at the top of the list. However, since mid-2015 conditions

have changed. With the aim of combating deflation, the ECB is purchasing bonds in open market transactions: as a result, the prices of such securities have risen, while their yields have fallen. This measure is favourable to holders of bonds purchased at an earlier time, but has reduced the average yields on roll-overs and new purchases of government bonds to around 1% or even less. It is therefore understandable that possession of such instruments fell from 21.7% of the sample in 2012 to 14% in the sample for early 2016.
The 2016 Survey indicates that as bondholders have declined, the preference for asset management instruments has increased. In 2015 total assets under management rose from 1,590 billion euro to 1,830 billion euro (Assogestioni).
Twenty-four percent of interviewees stated that they have chosen this option "to entrust their savings to experts and not worry about it anymore, making their lives simpler"; for 21.9% of investors, asset management offers better yields than "do-it-yourself" investing. At the same time, the turnover in asset management is declining as such investments become long-term companions. The combination of the priority on safety and the extreme volatility of equity markets which, in the final analysis, have not been growing and are without direction since the end of 2014, has intensified disenchantment with the equity market in the sample. Just 5.3% stated that they have purchased and/or sold shares in the past five years, a percentage that has fallen constantly since 2003, when it was 31.9%.

- **Zero rates are driving a preference for cash, but a persistent zero rate scenario could give rise to a change in the preferences of investors, who are willing to sacrifice liquidity but not security.** Since yields on less liquid assets are near zero, the percentage of assets held in liquid form in bank accounts is high. Nearly one interviewee out of five in the general sample (18.4%) keeps all of their assets liquid, whereas 9.1% hold more than half in cash and an additional 9% hold more than 30%. However, persistent zero rates could result in investors' sacrificing liquidity in search of alternative investments, such as real estate.

Low rates and volatility: back to real estate

- **An additional survey of 567 small investors, focusing on ways to invest with zero rates.** First of all, zero interest rate conditions are new to small investors, because this is the first time they have been in place since 1959: hence investors do not remember or have experience with this type of market. Secondly, the ECB's guidance indicates that yields will remain low for as long as necessary to combat deflation. Thirdly, low and zero rates affect both the returns on financial assets (like bonds and deposits) and borrowing costs (such as interest on mortgages and other loans). On the basis of these considerations, in 2016 the survey was expanded to include an additional sample of 567 investors aged 29 to 55 who held some form of investment. Through Doxa, they were given a different questionnaire, aimed at inquiring into their investment habits in an environment of persistent deflation and low or zero interest rates, with a particular focus on their willingness to switch from financial investments to real investments such as homes.

- **With zero rates, homes and cash deposits polarise investments.** The sample provided clear indications. Faced with a scenario of zero (or almost zero) rates for several years, interviewees responded that they intended to adopt polarised behaviour, by essentially concentrating on two choices: the choice to hold liquidity (chosen by 32% of investors) and the choice to invest in real estate (29% would consider purchasing a home for themselves and 20% the purchase of a home to rent out). The former appear to be motivated by the intention neither to lose nor gain money with riskier investments and by the expectation that zero rates will end sooner or later, and that would be the right time to resume investing. The latter seem to express a preference for a potential real-estate purchase, driven not only by economic variables, but also by needs that have gone unsatisfied or simply by the aspiration, long harboured by Italians, for a better home. The two groups of investors are distinguished, at the opposite ends of the spectrum of possible choices (total liquidity or total illiquidity), primarily by the aspect of income and by a savings reserve of more than one year's net income. These are factors that increase the propensity for real investment.

- **The riskiest choices and alternatives are marginal.** Only a limited proportion of the sample of small investors (8%) would react to zero rates by increasing their risk exposure, i.e., by investing in equities, currencies and derivatives. This attitude is consistent with economic theory: changes in possible combinations of risk and return on the market, and in particular a reduction of yields across the entire risk spectrum, do not change the willingness of investors to lose part of their investment, because this variable depends not on the market, but on each investor's income, assets and psychology. Changing one's "risk habitat" solely because market conditions have changed might easily prove an incorrect move in hindsight. Finally, 12% would purchase gold and precious metals and 4% would buy artwork. The search for alternative yields in this class of investment is minimal and driven by different economic and behavioural scenarios. Those who turn to gold show an undercurrent of unarticulated fear and general mistrust of the financial markets ("after zero rates, who knows what might happen next?"). Moreover, this mood tends to recur in all classes of investors, because some indicators show that, while individuals perceive falling prices (with the exception of healthcare services and a few other things, like utility bills), there is an equally widespread impression that when prices rise, the increases exceed those measured by official statistics. Those who turn to art (4%) generally have a complex, well diversified portfolio of assets and are taking advantage of the zero yield opportunity to purchase a work of art, essentially because the opportunity cost of doing so has momentarily decreased.

- **Housing: the market that Italians know best.** Small investors also turn to housing because this is the investment market of which they have the most direct knowledge, and in which they are probably the most interested. Information is indeed always an element that mitigates investment risk, since it means that investment decisions are better informed. As many as 46% of interviewees stated that they know the housing market and regularly check prices. The real-estate market is followed, at some distance, by the bond market (followed by 33% of the sample), and then by the stock exchange (24%) and the gold market (19%).

- **The search for homes also corresponds to a search for returns**. To return to the propensity to purchase real estate, those who are interested in approaching this market (but have not yet decided to) have a clear profile. In general, they have set aside cash or other liquid investments equivalent to more than one year's income (48%). They have also realised that the market for everyday consumer products is deflationary, contributing to compressing long-term returns on financial investments. However, this is not compatible with their aspiration to earn an average annual net profit of 2.6% from their investments in the next five years. Accordingly, foremost among the reasons why "purchasing real estate could be advantageous" are economic considerations, i.e. the conviction that they would be investing in a "reference asset" that retains its value over time (25%), followed by the possibility to "take advantage of the period of low prices" (17%) and the fact that income from the property, i.e. the rent collected or saved, is more than what a bank or a bond would provide (13%). In addition, 19% believe that home prices will increase in the next few years and 14% aim to take advantage of the unusually favourable mortgage conditions.

- **Potential new home buyers make up between 11% and 19% of the sample.** Economic variables are not the only reasons for investing in real estate. Those who are considering a purchase often aspire to a better home (43%) or have an effective need for a larger dwelling (29%). Potential buyers in the next three years (who account for between 11% and 19% of the sample) would primarily use their new homes for themselves, considering them as assets to enjoy and perhaps hand down to their children. Up to 8% of the sample could change homes but opt to rent, although positive views of rent make up one-third of the total, and are thus outnumbered by negative views. What is holding potential buyers back? For the time being, the stumbling block is the convalescent weakness of the secondary market, i.e. the fear that they will not be able to sell their current homes or obtain a sufficient price to make the qualitative leap. In other words, as the real-estate market becomes more liquid and the time needed to sell used homes decreases, potential new home demand will turn into actual demand.

- **A second home in the works for 9% of the additional sample**. The ongoing recovery of the housing market is real, but it is progressing slowly. The environment for second homes also appears to be changing. Nine percent of investors intend to buy in the next three years, with the awareness that second homes are almost never a sound investment. Proof of this may be seen in the fact that 74% of them have positive opinions of owning a second home, but only 22%, or fewer than one of three, consider second homes economically beneficial.

- **Investing in homes to be rented out is a good idea, but not a great one.** Homes, which deflation is once more making the main aspiration of a significant share of small investors, are not only to be lived in, but also to be rented out. With rates falling to zero, rental income is once again competitive. The share of investors interested in purchasing a home to rent out (20%) is smaller than that of investors interested in purchasing a home in which to live (29%), but still represents one-fifth of the sample, which is a larger share than that of current bondholders. There is no shortage of obstacles to putting this idea into practice and most of them relate to tenant selection, which is obviously an unknown. Then there is the tax issue. Homes to be rented out are by definition "second homes" and their tax treatment largely reflects this, from full register tax to municipal property tax and the inability to deduct renovation costs.

- **Gifts from the taxman: 41% of small investors are held back by tax conditions.** If they could ask the tax authorities for something, 59% of the sample would opt for a better balance between property taxes and taxes on other types of assets. However, this majority preference is not necessarily linked to imminent property transactions, but more to demand for equal tax treatment of assets. It should be recalled that the Italian government has already accommodated such requests by reducing taxes on first homes. However, the requests of the remaining 41% of the sample also bear emphasising. In fact, such requests hint at property transactions or suggest "frozen" potential demand in the housing sector. Fourteen percent of the sample would like to see a decrease in registry tax on rental properties; 13% would like a tax credit for selling and purchasing a first or second home in the same year; 9% would like to deduct a mortgage on a second home to be rented out; and 6% would like to deduct the mortgage on a second home for personal use. The appetite for home purchases could be much higher than declared (between 11% and 19%) if the tax treatment of real-estate investments were rendered less onerous.