WORLD ECONOMIC FORUM

COMMITTED TO IMPROVING THE STATE OF THE WORLD

Global Agenda Council on the Future of Insurance and Asset Management

Strengthening the Real Economy

Harnessing the Power of Long-Term Investors

Background

The world economy is growing, but far below its potential. There is a simple reason: We invest too little, or more precisely, we invest too little in our future.

Surprisingly, capital is not the bottleneck. Quite to the contrary, capital is plentiful. Some even talk about a savings glut. But most of it goes into financing public debt, rising house prices or share buybacks. Only a trickle finds its way into productive investments. The consequence: stagnating productivity, high unemployment and rising inequality.

There is no easy way out of this investment trap. Traditional policy tools have been tried but without much success: Fiscal policy is constrained by high debt burdens and monetary policy – after years of relentless expansion – becomes more and more ineffective. It's time to try another route.

This is the challenge facing the Global Agenda Council (GAC) on the Future of Insurance and Asset Management. Long-term Investors (LTIs) like insurers, pension funds, endowments and foundations, sovereign wealth funds, and traditional asset managers, don't have the silver bullet. But with 70 trillion euros in assets under management – or a third of all financial assets worldwide – they can certainly contribute to lasting solutions. Even more so as banks retrench as traditional lenders.

But frustratingly, LTIs have not unleashed their full potential. In fact, when it comes to in our future well-being and supporting vibrant economic growth (be it sustainable energy, infrastructure or new technologies) their profile as enablers is rather low. This is a pity. It deprives the economy of much needed long-term risk capital and it condemns LTIs to earn low returns, aggravating the looming pension threat.

For sure, there are many LTIs trying to channel funds into, say, infrastructure. This is welcome. But showcase investments alone won't revive the economy or avert the pension crisis. We need a new mindset and framework to transform LTIs role in our economies and societies fundamentally.

LTIs are fundamentally different from short-term market players and offer abilities that are in short supply these days. LTIs actually *absorb* risks. Therefore,

- LTIs foster financial stability by holding assets through economic cycles, stabilizing markets, not rushing to the exit.
- LTIs foster growth by being long-term reliable risk-takers that are essential for investments and innovations, the main drivers for economic progress and prosperity.
- LTIs foster social stability by shielding their clients from financial risks associated with old-age provisions.

This potential should be used to its fullest. To understand the constraints holding back LTIs, the GAC conducted 50 interviews with senior representatives of governments, regulators, academia, and the LTI community.

Challenges and Call to Action

These interviews revealed four challenges:

- Efforts to stabilize markets – mainly by central banks providing unlimited and free liquidity – has created new uncertainty: risks are no longer adequately priced.
- The new regulatory landscape is highly complex and does not fully reflect differences in business models: One size does not fit all – especially when it is modeled on banking regulations. The result is an artificial increase in short-term volatility in many LTIs' balance sheets, creating a bias for more short-term and pro-cyclical investments.
- Market structures are often underdeveloped, be it credit markets, securitizations, or infrastructure. For example, limited standardization or tradability of assets put a damper on LTIs' productive long-term investments.
- Ineffective coordination among LTIs themselves and too little fact-based involvement limits LTIs' voice in the policy-making process. Instead of advancing common societal interests, lobbying efforts are largely uncoordinated.

These constraints cannot be eliminated easily. Radical action is required. Just tinkering with the calibration of risk charges will not do the trick. We need:

- Regulations that accurately reflect how LTIs are systemic stabilizers, not systemic risks.
- A legal framework that protects LTIs over long risk horizons.
- New accounting standards that reduce volatility and pro-cyclicality.
- A global, tradable asset class of infrastructure.

To make this happen, LTIs themselves must collaborate better to advance their beneficial role as economic drivers. We need to speak with one voice. Only then, can we lay the groundwork for new public-private partnerships and finance future growth.

Let's make Davos 2016 the start of this new collaboration!

Contact Information

Oliver Bäte
CEO Allianz SE, GAC Chair

Dr. Arne Holzhausen
Group Economic Research, Allianz
Arne.Holzhausen@allianz.com

Anne Richards
CIO Aberdeen Asset Management, GAC Vice Chair

Lorraine Kay
CIO Office Aberdeen Asset Management
Lorraine.Kay@aberdeen-asset.com

Abel Lee
World Economic Forum's Director of Insurance of Asset Management
Abel.Lee@weforum.org

Alexandra Durbak
Council Manager of the GAC on the Future of Insurance and Asset Management
Alexandra.Durbak@weforum.org