INSTITUTIONAL INVESTORS AND LONG TERM INVESTMENT

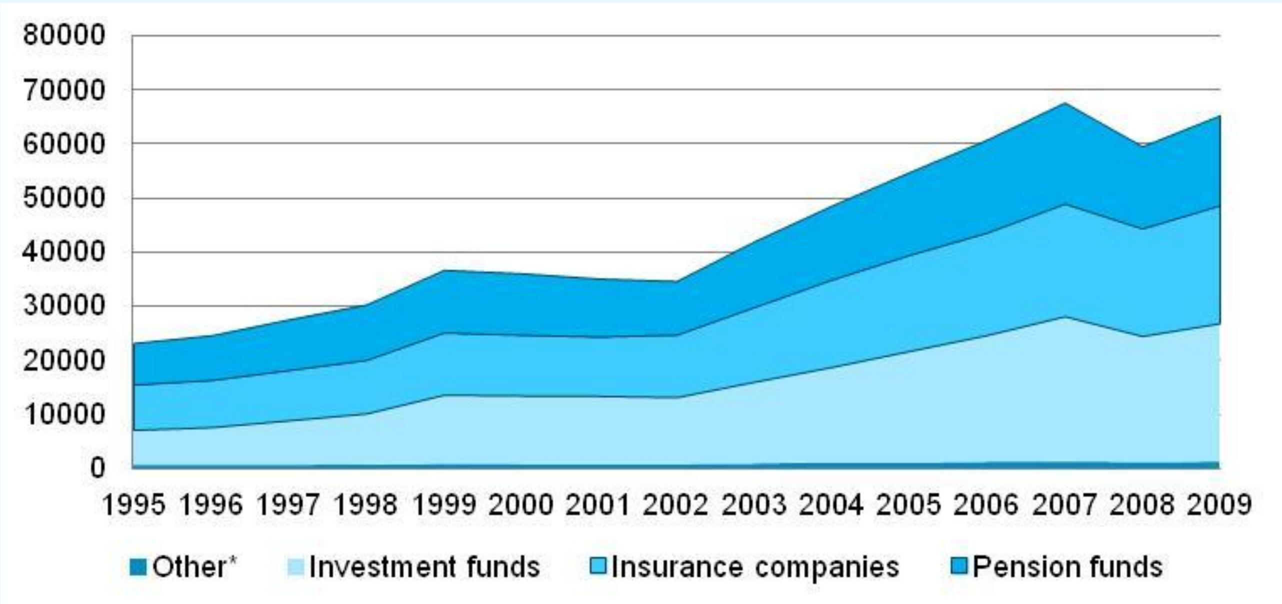
TAKING THE RESEARCH AND POLICY AGENDA FORWARD AT THE OECD

The increasingly short supply of long-term capital since the 2008 financial crisis has profound implications for growth and financial stability. This OECD project, which runs through 2013 will develop research and identify and promote policy options to encourage institutional investors to act in their long-term capacity.

What do we mean by long-term investment?

The main institutional investors in the OECD - pension funds, insurance companies and mutual funds - held over US$65 trillion at the end of 2009. The potential for the institutional investor sector in emerging economies is also growing fast, with Sovereign Wealth Funds, (which held over US$4 trillion at the end of 2009) currently being the most important source of capital in these countries. The long-term nature of these investors' liabilities should, in theory at least, encourage them to invest with a long-term perspective in mind.

Figure 1. Relative share and total assets by type of institutional investors,1995-2009 (USD billions)



* Other forms of institutional savings include foundations and endowment funds, non-pension fund money managed by banks, private investment partnership and other forms of institutional investors.

Source: OECD Global Pension Statistics and Institutional Investors databases, and OECD estimates.

Selected reports

Available online at www.oecd.org/daf/fin

- Promoting long-term investment by institutional investors
- Fostering long-term investment and economic growth: summary of a high-level OECD financial roundtable
- Pension funds investment in infrastructure: a survey
- Pension funds investment in infrastructure: policy actions
- The role of pension funds in financing green growth initiatives
- Sovereign debt challenges for banking systems and bond markets
- Improving financial education and awareness on insurance and private pensions
- Infrastructure to 2030: telecom, land transport, water and electricity
- Engaging the private sector in African infrastructure
- Corporate governance lessons from the financial crisis
- Fostering innovation for green growth

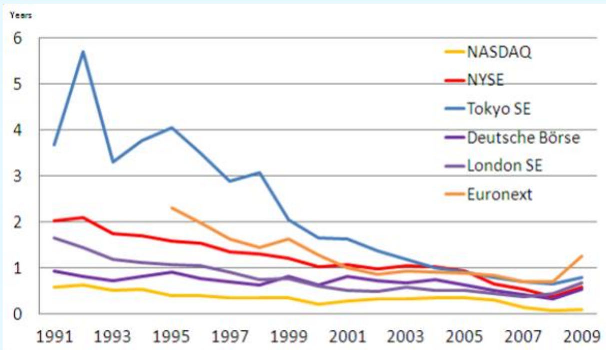
Statistics

- Global Pension Statistics
- Insurance Statistics Yearbook
- African Central Government Debt Statistical Yearbook
- Central Government Debt Statistical Yearbook

Why is long-term investment important?

- **Patient capital** allows investors to access illiquidity premia, lowers turnover, encourages less pro-cyclical investment strategies and therefore higher net investment rate of returns and greater financial stability.
- **Engaged capital** encourages active voting policies, leading to better corporate governance.
- **Productive capital** provides support for infrastructure development, green growth initiatives, SME finance etc., leading to sustainable growth.

Figure 2. Average holding period – selected exchanges



Source: OECD Corporate Affairs Division

What are the issues?

Despite the potential benefits of long-term investment, institutional investors are often being labelled as 'short-term' – as evidenced by declining investment holding periods, growing allocations to high-turnover investment vehicles and insufficient engagement in terms of corporate governance.

At the same time, the largest investors are increasingly looking for "alternative" investment opportunities to the traditional asset classes (equity and bonds), to ensure portfolio diversification and provide stable, inflation-protected cash flows. Infrastructure is increasingly emerging as an attractive investment, but its growth is sometimes hindered by inadequate institutional and regulatory frameworks.

What are the solutions?

The OECD believes that policy reforms can be used to encourage institutional investors to play a longer-term role. Such reforms could include:

- Improving the regulatory framework for institutional investors - such as developing risk-management systems to take account of longer term risks, removing investment regulatory barriers and addressing potential unintended short-term incentives in solvency and funding regulations.
- Policies to encourage active share ownership could also be pursued (including allowing collaboration, supporting international codes of practice and increased supervisory oversight of pension funds' investment mandates, fees, turnover and voting).
- A supportive policy framework developed (with long-term policy planning, tax incentives and risk transfer mechanisms). Addressing knowledge gaps on the part of institutional and retail investors, and regulators themselves will also be required.

What are we doing at the OECD?

The OECD project on long-term investing aims to develop research and identify and promote policy options, encouraging institutional investors to act in their long-term capacity through supporting stronger efforts in independent data collection, producing better research and disseminating good practices and case studies. More specifically, by:

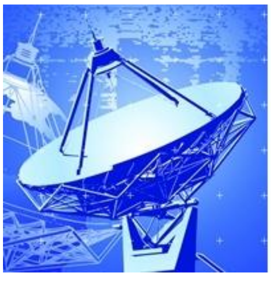
Monitoring LT institutional investors' asset allocation to infrastructure. This would be done through collection of data (on assets, flows, and performance, valuation methods, etc) directly from major pension funds, insurers, SWFs and other long-term investors. This would build on existing OECD work and databases.

Undertaking further research on related topics. Planned research papers in 2011-12 include:

- Life insurance and infrastructure investment
- The emerging market perspective on institutional investment in infrastructure
- Impact of solvency regulation and accounting standards on life insurers' and pension funds' investment strategies
- Institutional investors and corporate governance
- Institutional investors and debt bond markets.
- Pension funds and infrastructure: Canada vs. Australia.

Identifying and promoting policy options. Practical policy options, such as the solutions outlined above, would be developed to assist governments in improving the background and incentives for long-term investing in their countries.

Disseminating research and policy options through a series of high-level meetings and conferences. Policy impact would be targeted through the public sector and regulatory community and via industry contacts.





JOIN US IN THIS PROJECT

A centre for international research, analysis and dialogue

The OECD has for many years led an international research and policy agenda on institutional investors (as part of the Programme of Work of its Insurance and Private Pensions Committee and the Committee on Financial Markets). The OECD is also the leading international organisation in terms of the collection and analysis of statistics and indicators on institutional investors with products such as Global Pensions Statistics, Global Insurance Statistics and the Institutional Investors Database.

Our initial work on long-term investing has been summarised in a discussion note 'Promoting Longer-term Investment by Institutional Investors: Selected issues and Policies', which has received extensive coverage and been discussed at high-level meetings of policy makers and investment industry representatives.

This new project brings together OECD in-house expertise on institutional investors (through work on financial markets and institutions, insurance companies, pension funds and debt management) with a broader policy agenda on long-term Investment issues, covering a range of initiatives – on Green Growth, Foreign Investment and Capital Flows, Corporate Governance, Private Sector Development, Financial Education, etc.

The project involves close co-operation with national policymakers, private sector representatives and academia, as well as other international organisations and governmental bodies, such as the International Organisation of Pension Supervisors and the International Association of Insurance Supervisors, the International Organisation of Securities Commissions and the World Bank. The OECD's ability to convene high-level representatives from different stakeholder groups to its meetings and its cross-thematic research capability will be key project strengths.

The OECD welcomes private sector stakeholders to join us in this project.

This project offers our partners:

- Access to a broad range of leading edge research on the barriers and solutions to long-term investing;
- The ability to contribute to the policy debate on long-term investing - on both a national and international level;
- Access to policy makers and regulators through regular meetings.

If you are interested in joining us in this project, please contact

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