

Dynamics and potential for the development of the certificates market in Italy

Bocconi



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Diffusion and perception of certificates among investors and financial advisors in Italy: an empirical analysis

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Introduction

- Despite their limited diffusion in Italy, certificates offer investors a great opportunity to diversify their investment portfolios. In order to get a deeper understanding of the potential for the development of the certificates market in Italy, Newfin and Enter (two Bocconi research centers) together with ACEPI (an Italian association of certificates issuers) conducted a research whose results were presented during a conference held at Bocconi University on November, 8, 2007.
- The main research objectives were: to analyse investors' knowledge and perception of certificates both by interviewing them directly (192 interviews), and by asking financial advisors (72 online surveys); to identify pro and cons of investing in certificates. Furthermore, the study analysed characteristics and future growth rate of the certificates market in Italy.

Index

- Section I - Potential Investors
 - **Introduction & Sample**
 - A – Portfolio structure
 - B – Knowledge of certificates
 - C – Evaluation of some ideal-types
 - D – Comparative perception of investment products

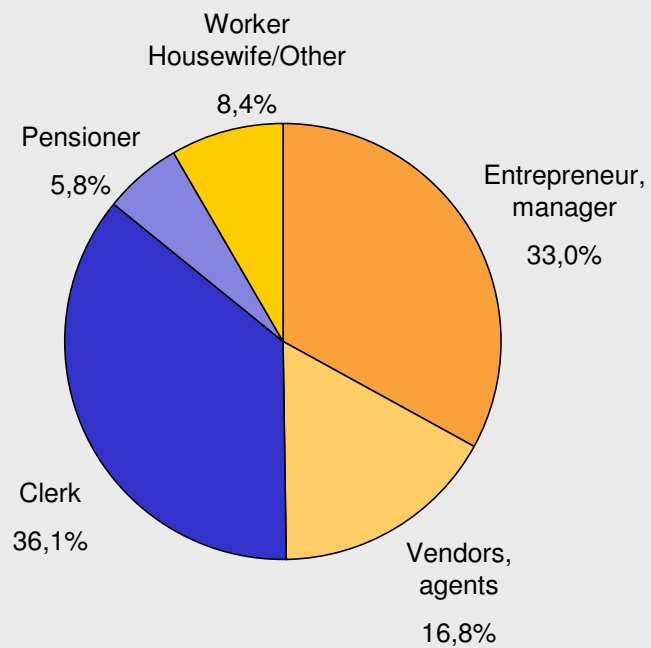
- Section II - Financial advisors and their perceptions of certificates and investors
 - Introduction & Sample
 - A – Consumers' investment preferences (according to financial advisors)
 - B – Information sources
 - C – Market scenarios according to the advisors' view

Introduction

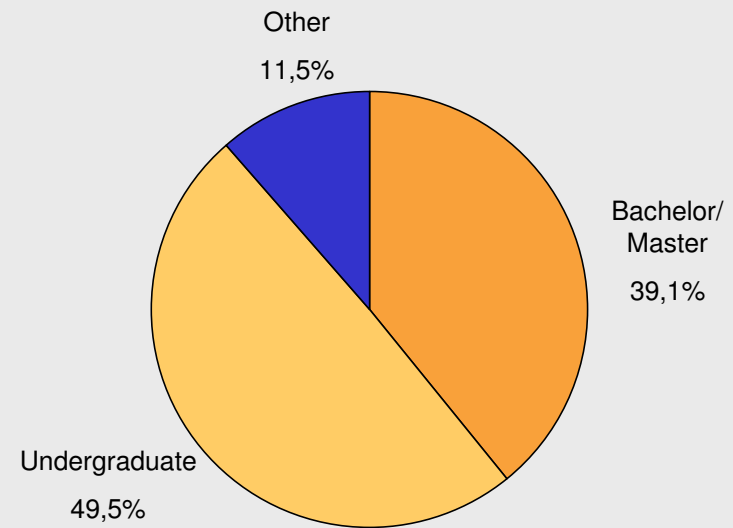
- First empirical analysis on investors' knowledge of certificates and on their willingness/unwillingness to invest in them
- Target: 192 common investors (not self-directed). Period: August-September
- Areas of investigation:
 - Portfolio decisions
 - Knowledge of certificates
 - Evaluation of specific categories of certificates
 - Comparative perception of risk/return

Sample – Investors Retail

Work

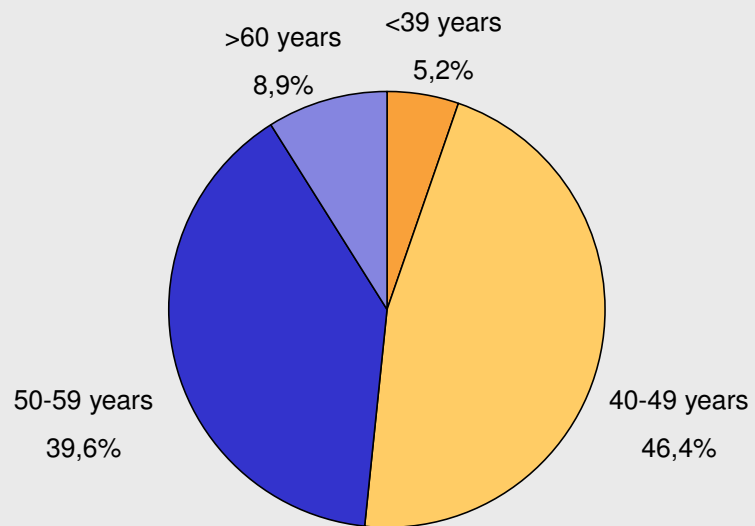


Education

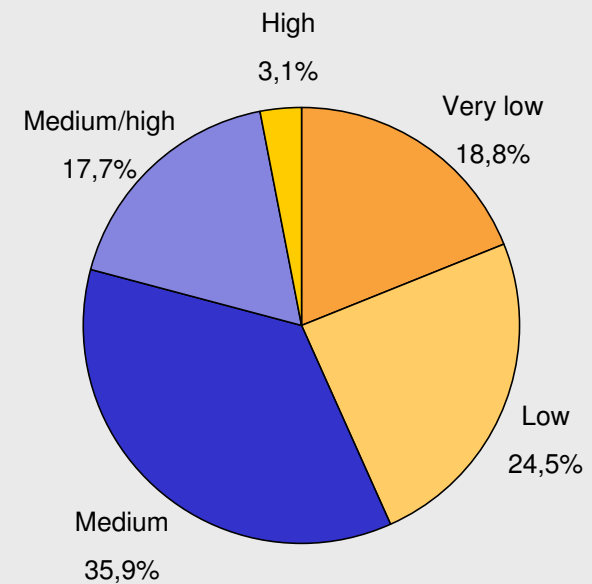


Sample – Investors Retail

Age



Previous investment experience (self-evaluation)



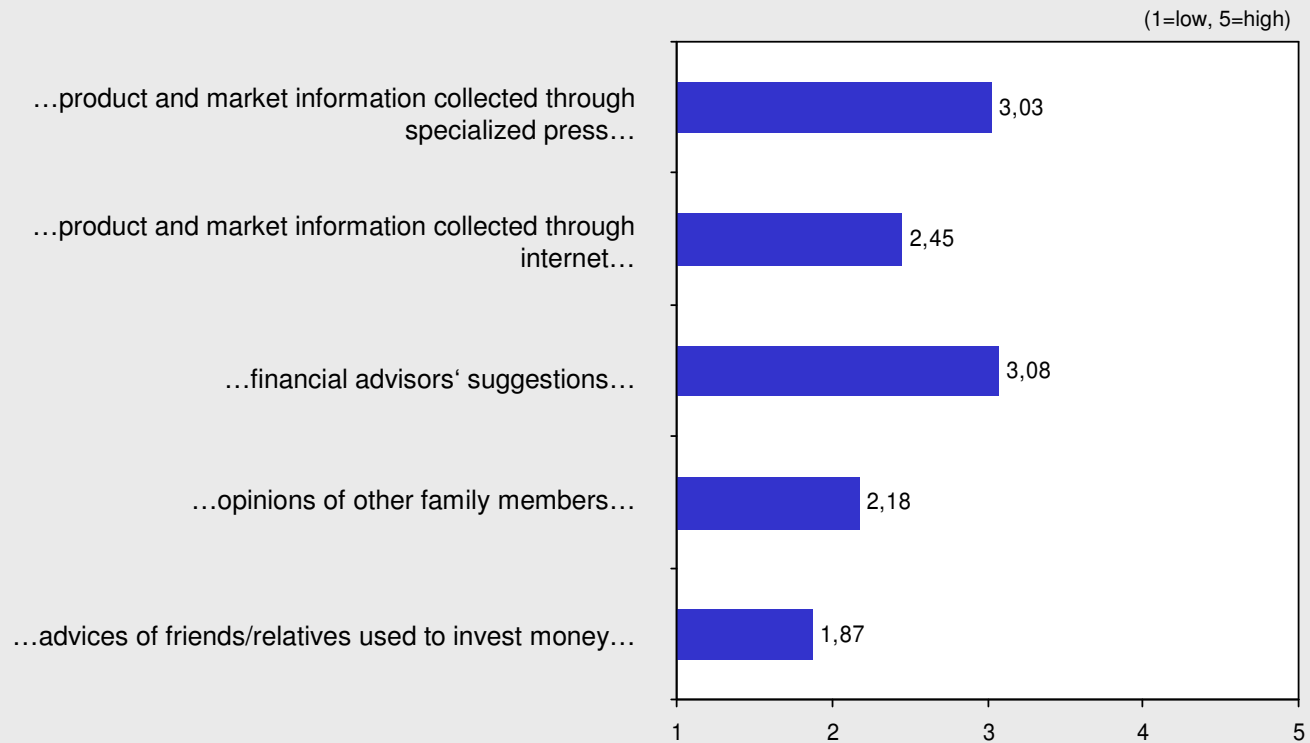
Index

- Section I - Potential Investors
 - Introduction & Sample
 - **A – Portfolio structure**
 - B – Knowledge of certificates
 - C – Evaluation of some ideal-types
 - D – Comparative perception of investment products

- Section II - Financial advisors and their perceptions of certificates and investors
 - Introduction & Sample
 - A – Consumers' investment preferences (according to financial advisors)
 - B – Information sources
 - C – Market scenarios according to the advisors' view

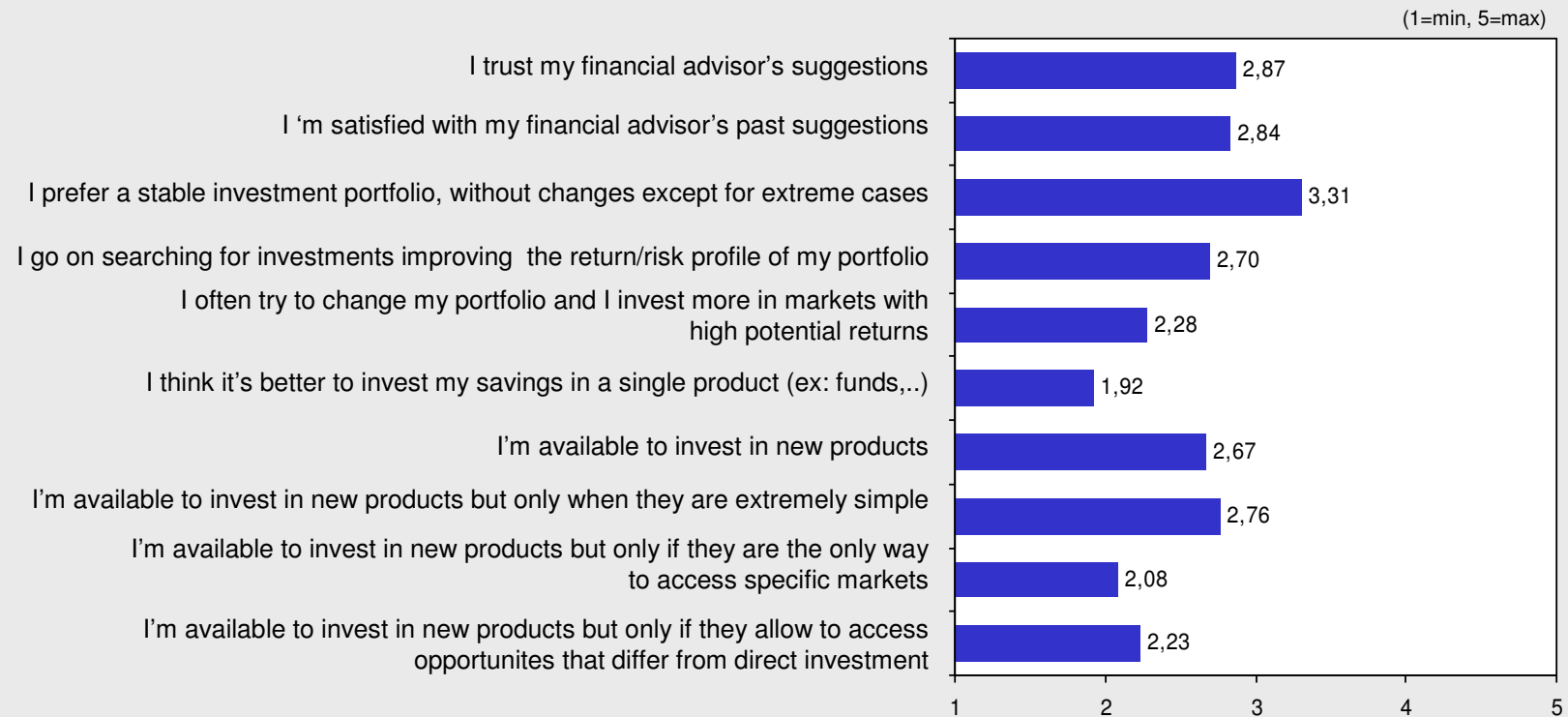
A – Portfolio structure

When structuring your investment portfolio, what's the influence of:



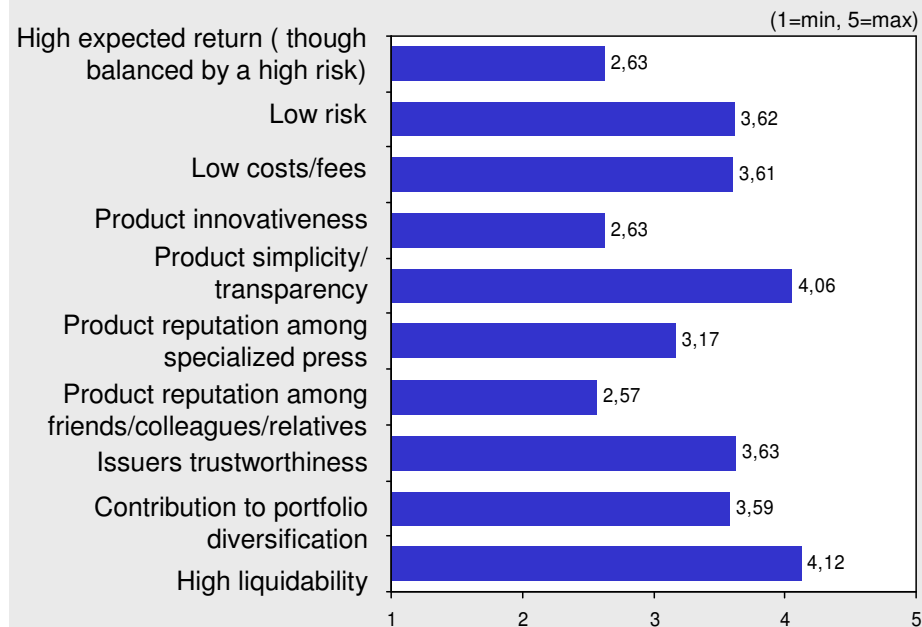
A – Portfolio structure

How much do you agree with the following statements?

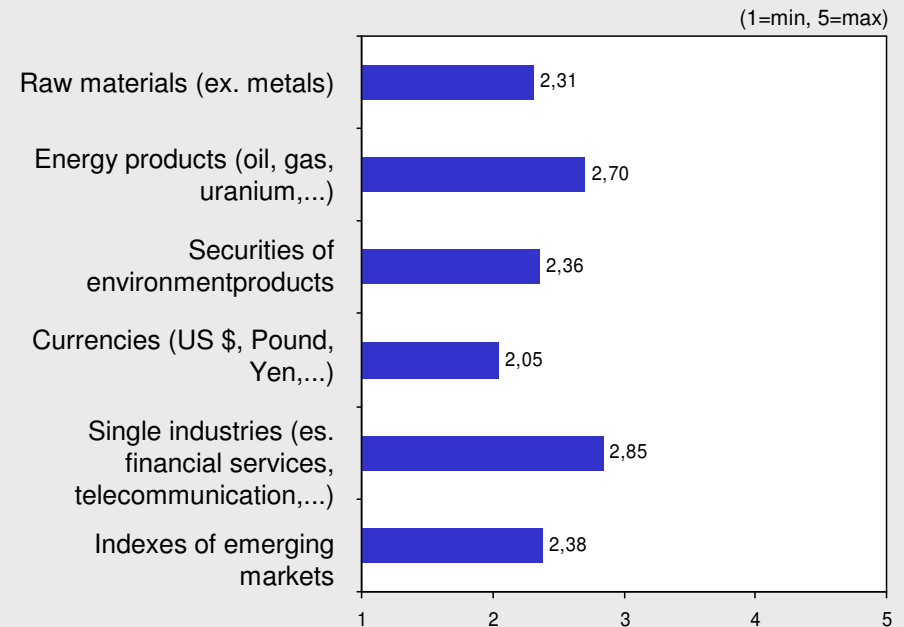


A – Portfolio structure

How much do you value these characteristics when choosing an investment product?



How much are you interested in investment products with the following underlyings?



A – Portfolio structure

Preliminary insights

- Strong tendency to delegate investment decisions to financial advisors, though without trusting them (trust in friends' advices and self-evaluation is even lower)
- Resistance to change/innovation: product innovativeness is not a plus
- Though appreciating diversification, the possibility to access differentiated markets/returns is not exploited
- Low self-confidence pushes investors to choose standard and simple products

Index

- Section I - Potential Investors
 - Introduction & Sample
 - A – Portfolio structure
 - **B – Knowledge of certificates**
 - C – Evaluation of some ideal-types
 - D – Comparative perception of investment products

- Section II - Financial advisors and their perceptions of certificates and investors
 - Introduction & Sample
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 - B – Information sources
 - C – Market scenarios according to the advisors' view

B – Knowledge of certificates

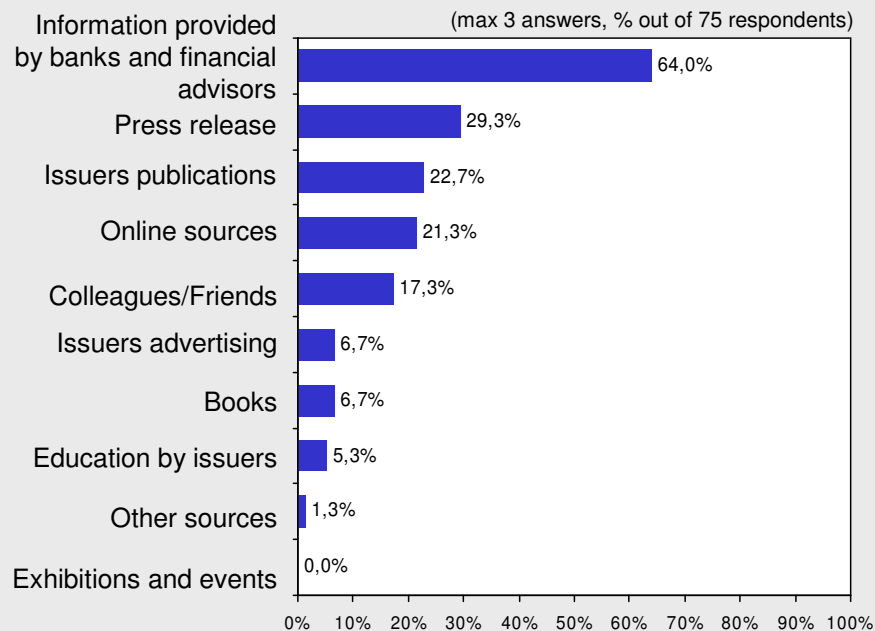
Do you know certificates as investment products?

	N.	%
Yes, I know them well	40	20,8%
I heard about them but I don't know their main features	62	32,3%
No, I don't	90	46,9%

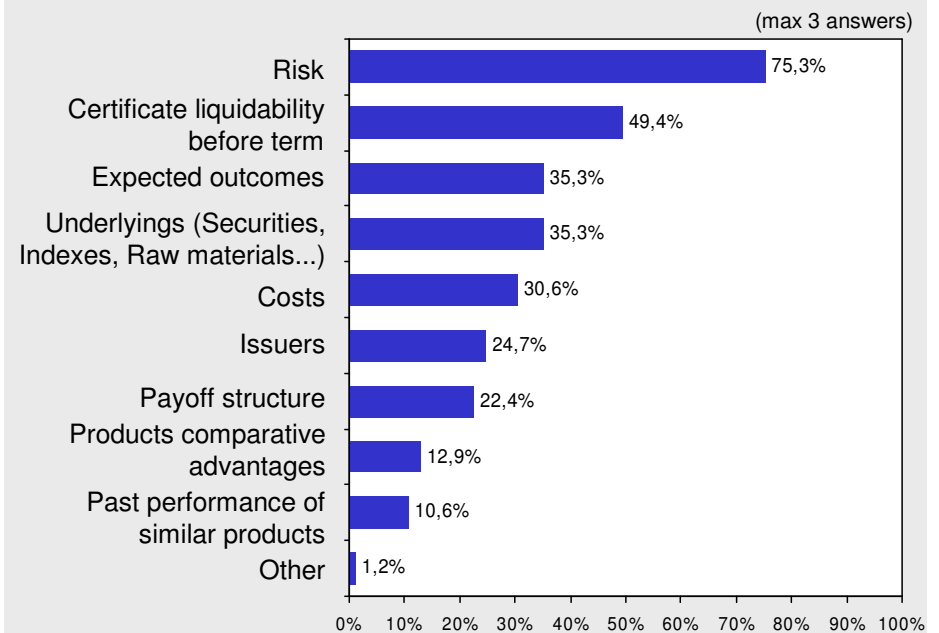
- About 75 interviewed people (39%) felt able to go on with the survey and answer following questions

B – Knowledge of certificates

How did you develop knowledge about certificates?

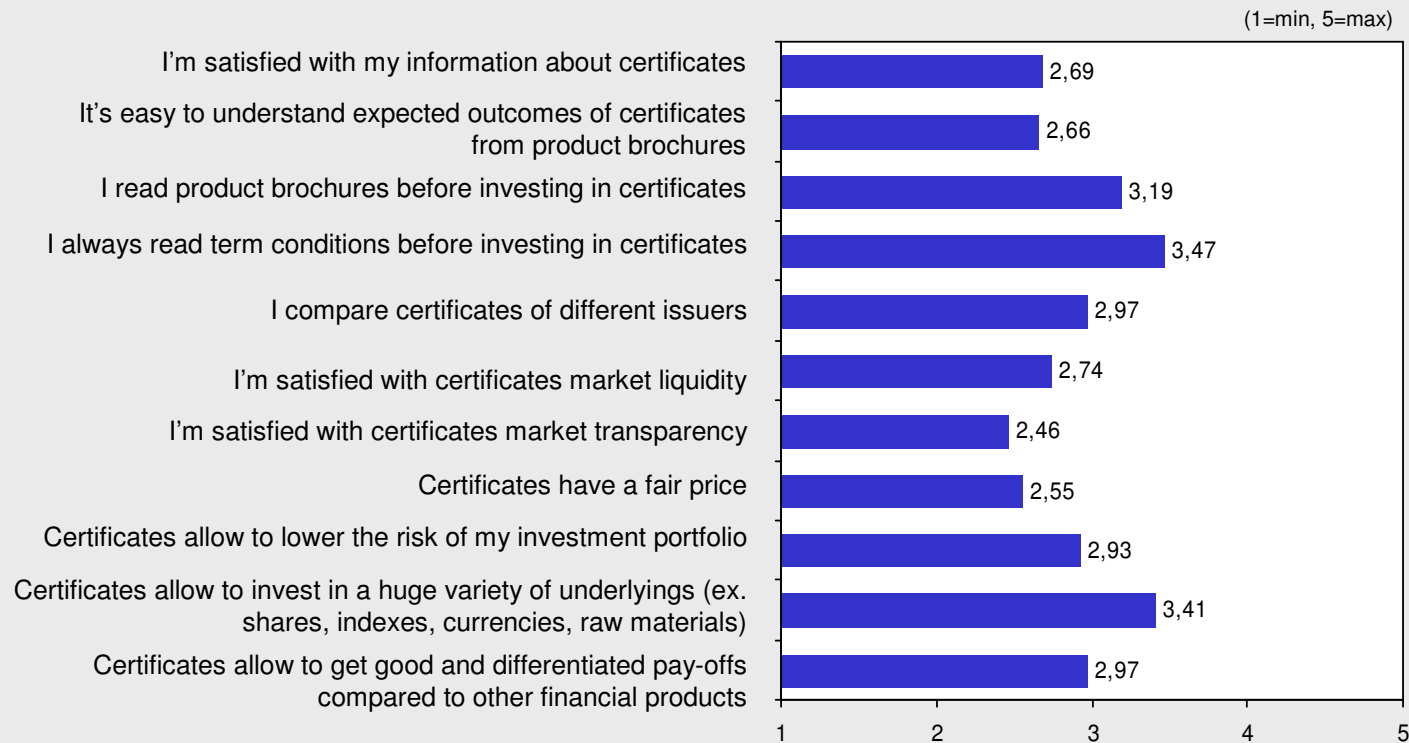


If you should buy a certificate, what are the information you would like to receive?



B – Knowledge of certificates

If you know certificates, how much do you agree with the following statements?



B – Knowledge of certificates

Which certificates do you know?

Certificate type	N.	% out of 102 (full partial knowledge of certificates)
Benchmark	43	42,2%
Equity protection	25	24,5%
Bonus	19	18,6%
Turbo/Shot, Minifutures, Wave	15	14,7%
Discount	15	14,7%
Airbag	12	11,8%
Twin Win	11	10,8%
Outperformance	8	7,8%
Cash collect	8	7,8%
Butterfly	8	7,8%
Double up, Double chance, Super Stock	4	3,9%
Pepp	3	2,9%
Express	2	2,0%
Other	5	4,9%
<i>I know at least 1 certificate</i>	<i>63</i>	<i>61,8%</i>
<i>I know at least 2 certificates</i>	<i>53</i>	<i>52,0%</i>
<i>I know at least 3 certificates</i>	<i>31</i>	<i>30,4%</i>

B – Knowledge of certificates

- The average degree of knowledge of certificates is not that low, given that more than 1 out of 4 interviewed people knows at least two typologies, 1 out of 5 says that he knows them well and more than the half of the sample says that they heard about them
- Information is mainly provided by financial advisors and banks; about 20-25% of investors knowing certificates, recognize the relevance of specialized press, issuers reports and online services
- Most of investors declare to read product brochures, but don't compare certificates of different issuers
- Most people search for information on certificates' risk and liquidability

Index

- Section I - Potential Investors
 - Introduction & Sample
 - A – Portfolio structure
 - B – Knowledge of certificates
 - **C – Evaluation of some ideal-types**
 - D – Comparative perception of investment products

- Section II - Financial advisors and their perceptions of certificates and investors
 - Introduction & Sample
 - A – Consumers' investment preferences (according to financial advisors)
 - B – Information sources
 - C – Market scenarios according to the advisors' view

C – Evaluation of some ideal-types

- In the following section, investors have been exposed to some certificates payoffs (without naming them) and asked an evaluation

- The three proposed typologies are:
 - equity protection (2 years)
 - bonus (2 years)
 - express (4 years)

C – Evaluation of some ideal-types

Certificates categories more in detail: (1) Equity protection

- Did you already buy this type of certificates? Yes, I did **27,7%**
- Would you be interested in investing in them? Yes, I would **63,0%**
- If you never bought a certificate or you are not interested in investing in them, why?

(max 3 answers, 98 respondents)

I don't see any potential advantage in investing in new products	42,9%
Low liquidability	24,5%
High risk	23,5%
Product complexity	20,4%
Huge costs	17,3%
Low expected returns	12,2%
Negative previous experiences with similar products	10,2%
Other	22,4%

C – Evaluation of some ideal-types

Certificates categories more in detail: (2) Bonus

- Did you already buy this type of certificates? Yes, I did **7,8%**
- Would you be interested in investing in them? Yes, I would **23,4%**
- If you never bought a certificate or you are not interested in investing in them, why?

(max 3 answers, 159 respondents)

High risk	55,3%
Product complexity	45,3%
I don't see any potential advantage in investing in new products	31,4%
Low Liquidability	15,7%
Huge costs	9,4%
Negative previous experiences with similar products	6,3%
Low expected returns	4,4%
Other	12,6%

C – Evaluation of some ideal-types

Certificates categories more in detail: (3) Express

- Did you already buy this type of certificates? Yes, I did **8,3%**
- Would you be interested in investing in them? Yes, I would **33,9%**
- If you never bought a certificate or you are not interested in investing in them, why?

(max 3 answers, 142 respondents)

Product complexity	52,1%
I don't see any potential advantage in investing in new products	33,8%
High risk	33,1%
Low Liquidability	15,5%
Huge costs	8,5%
Negative previous experiences with similar products	7,0%
Low expected returns	7,0%
Other	18,3%

C – Evaluation of some ideal-types

Propensity to invest and individual characteristics

Would you like to buy the product? % Yes	Equity protection	Bonus	Express
<i>...out of total respondents</i>	63,0%	23,4%	33,9%
...among graduates	68,0%	26,7%	40,0%
...among entrepreneurs, managers,...	71,4%	30,2%	44,4%
...among clerks	66,7%	26,1%	34,8%
...among high-experienced people	62,5%	17,5%	35,0%
...among low-experienced people	66,3%	24,1%	33,7%
...among people younger than 50	66,7%	25,3%	34,3%
...among people highly trusting in financial advisors	63,9%	24,6%	44,3%
...among people highly satisfied with previous financial advisors' suggestions	68,9%	32,8%	41,0%
...among more innovation-oriented people	62,0%	24,0%	42,0%
...among those who value liquidability 4 to 5	64,7%	24,7%	38,0%

C – Evaluation of some ideal-types

- For all of them, though in different degrees, there is a huge market potential; Many investors claimed that they never invested in those products, because they didn't know them
- Main fears about certificates as investment products are related to their high perceived risk and complexity, together with the perceived low liquidability
- Propensity to invest depends on investors' characteristics. Entrepreneurs/managers and graduated people seem to be more inclined to invest in certificates; low self-confidence

Index

- Section I - Potential Investors
 - Introduction & Sample
 - A – Portfolio structure
 - B – Knowledge of certificates
 - C – Evaluation of some ideal-types
 - **D – Comparative perception of investment products**

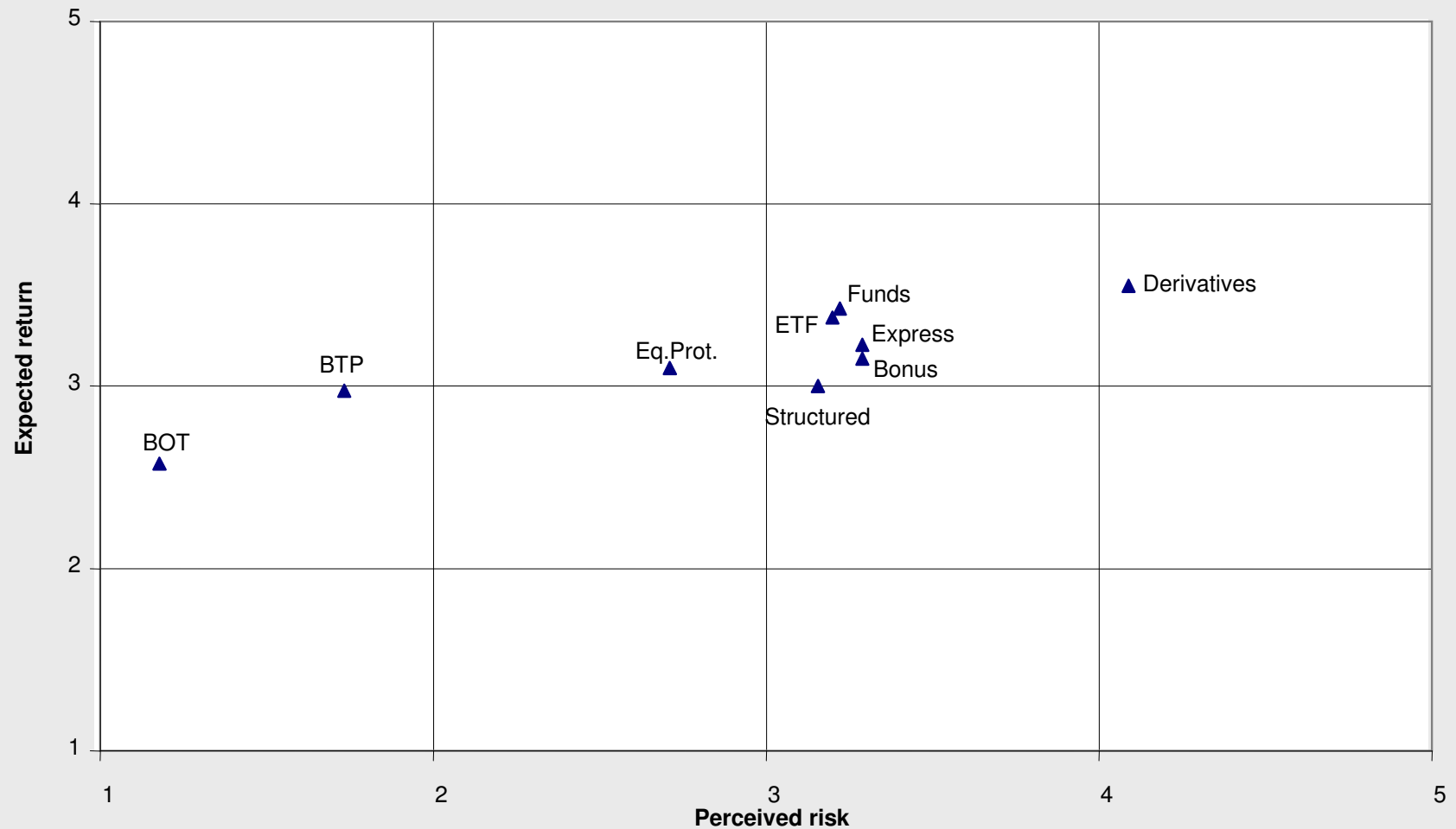
- Section II - Financial advisors and their perceptions of certificates and investors
 - Introduction & Sample
 - A – Consumers' investment preferences (according to financial advisors)
 - B – Information sources
 - C – Market scenarios according to the advisors' view

D – Comparative perception of investment products

- Final section asked to rate different products on a scale from 1 to 5 (BOT, BTP a 5 anni, ETF, mutual funds, derivatives, and the three certificates proposed with the names of Alfa, Beta and Gamma) in terms of expected return/risk/costs and transparency
- The first objective was to analyse how many investors were able to discriminate, the second to analyse perceptions of the three proposed certificates with respect to other products
- Only 40 out of 192 interviewed people have been able to evaluate all the products
- 90 interviewed people have been able to evaluate all the products but ETF and derivatives

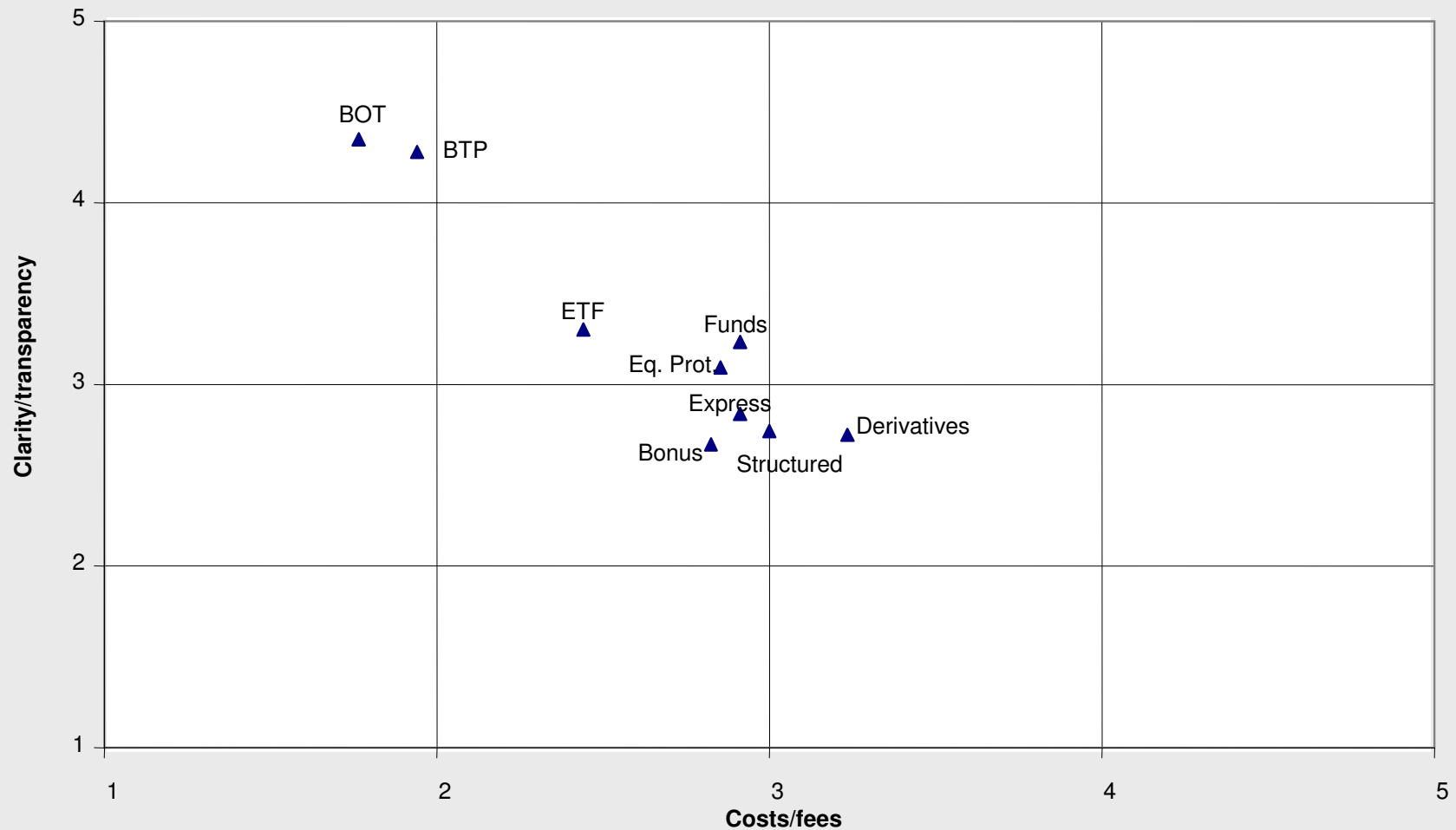
D – Comparative perception of investment products

Perception of the risk/return profile of alternative products



D – Comparative perception of investment products

Perceived costs and liquidity



Index

- Section I - Potential Investors
 - Introduction & Sample
 - A – Portfolio structure
 - B – Knowledge of certificates
 - C – Evaluation of some ideal-types
 - D – Comparative perception of investment products

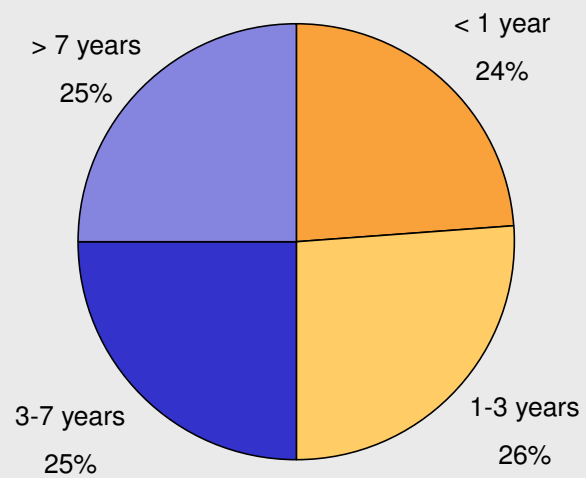
- Section II - Financial advisors and their perceptions of certificates and investors
 - **Introduction & Sample**
 - A – Consumers' investment preferences (according to financial advisors)
 - B – Information sources
 - C – Market scenarios according to the advisors' view

Introduction

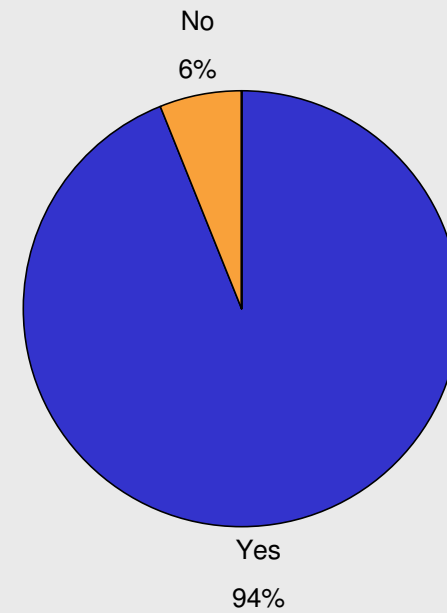
- This second section aimed at understanding:
 - Financial advisors' perception of certificates
 - Financial advisors' perception of investors' propension/unwillingness to invest in certificates
- Target: 72 financial advisors. Period: September – October
- Financial advisors were asked the same questions that had been asked to investors in order to check for similarities/heterogeneity
- Additional questions on:
 - obstacles to the development of the certificates market
 - initiatives to develop the potential certificates market
 - expected market growth rate for the next 5 years

Sample

How long have you been a financial advisor?



Do you sell products of different issuers?



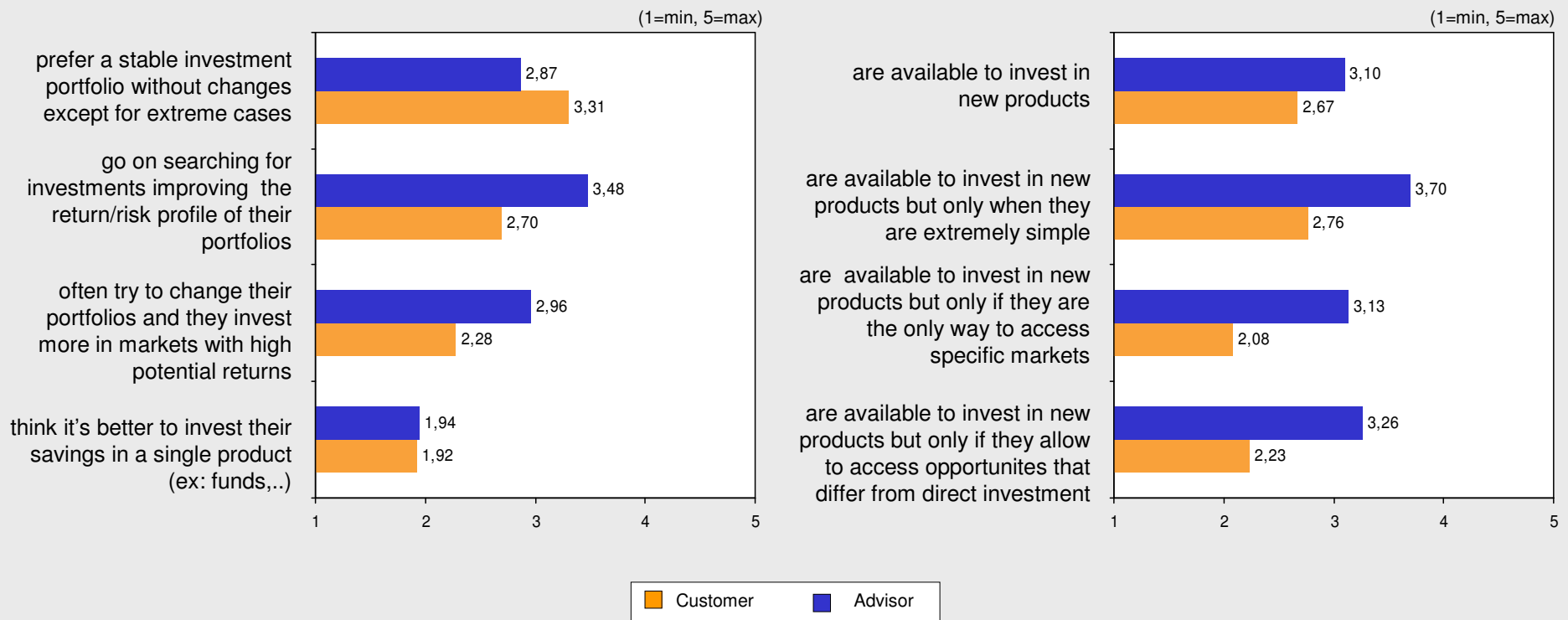
Index

- Section I - Potential Investors
 - Introduction & Sample
 - A – Portfolio structure
 - B – Knowledge of certificates
 - C – Evaluation of some ideal-types
 - D – Comparative perception of investment products

- Section II - Financial advisors and their perceptions of certificates and investors
 - Introduction & Sample
 - **A – Consumers' investment preferences (according to financial advisors)**
 - B – Information sources
 - C – Market scenarios according to the advisors' view

A – Consumers' investment preferences

My customers...



A – Consumers' investment preferences

Investment choice

- According to financial advisors, investors are less static and resistant to change/innovation than their self-perception
- This may be explained by the fact that those, followed by a financial advisor, are not average investors
- According to financial advisors product simplicity and diversification potential increase investors' propensity to invest in new products to a greater extent than declared by investors: this implies that potential benefits are not directly perceived but need to be explained

Index

- Section I - Potential Investors
 - Introduction & Sample
 - A – Portfolio structure
 - B – Knowledge of certificates
 - C – Evaluation of some ideal-types
 - D – Comparative perception of investment products

- Section II - Financial advisors and their perceptions of certificates and investors
 - Introduction & Sample
 - A – Consumers' investment preferences (according to financial advisors)
 - **B – Information sources**
 - C – Market scenarios according to the advisors' view

B – Knowledge of certificates

Information sources

	Financial Advisor	Investors
Information released by banks	91,7%	64,0%
Issuers publications	73,6%	22,7%
Education by issuers	23,6%	5,3%
Press release	27,8%	29,3%
Issuers advertising	8,3%	6,7%
Books	20,8%	6,7%
Online sources	25,0%	21,3%
Colleagues/friends	22,2%	17,3%
Exhibitions and events	4,2%	0,0%
Other	9,7%	1,3%

- Main role played by information provided by banks
- Increased relevance of issuers' documentation

B – Knowledge of certificates

What is relevant to buy them?

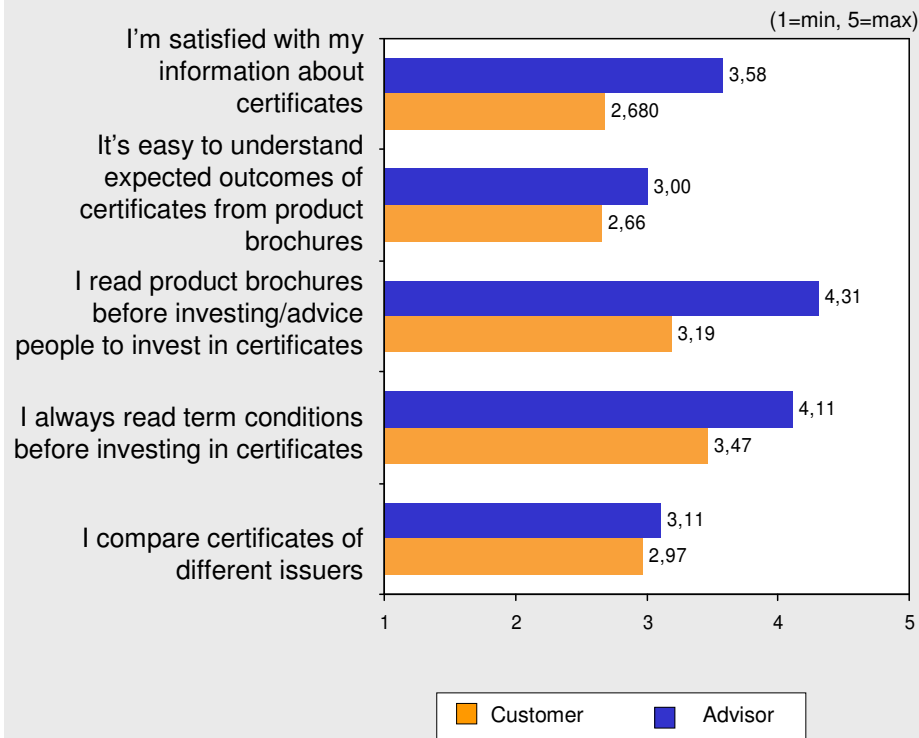
	Financial Advisor What are the main issues that your customers raise?	Investors If you should buy a certificate, what are the information you would like to receive
Risk	54,2%	75,3%
Liquidability	43,1%	49,4%
Expected return	43,1%	35,3%
Underlying	41,7%	35,3%
Costs	37,5%	30,6%
Payoff structure	22,2%	22,4%
Issuer	19,4%	24,7%
Products comparative advantages	20,8%	12,9%
Past performances of similar products	5,6%	10,6%
Other	9,7%	1,2%

For investors...

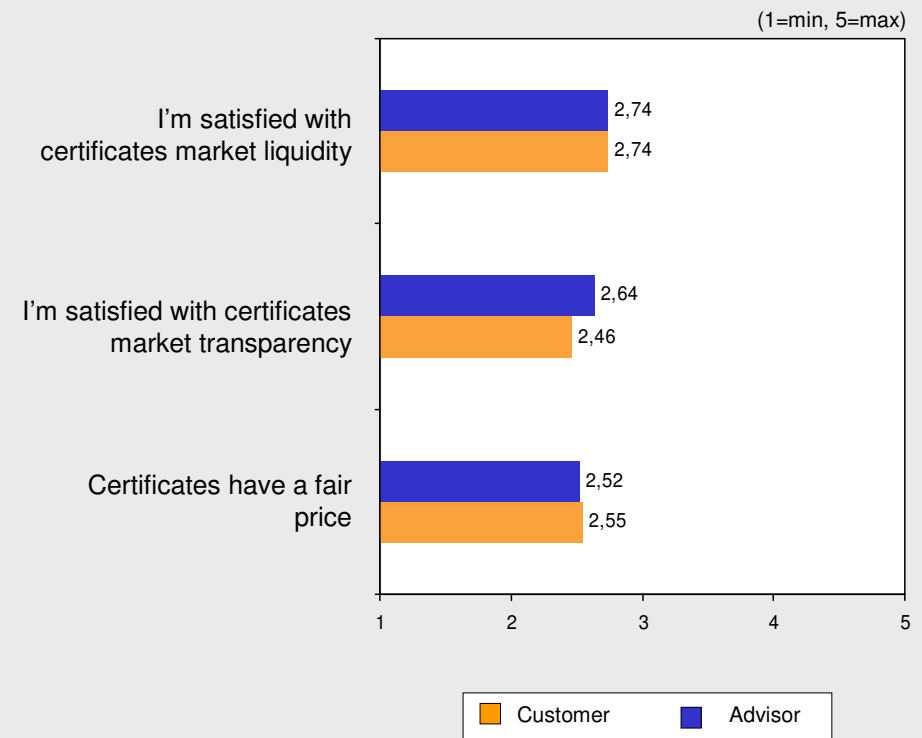
- ... more importance attached to risk (and issuers), less to expected return
- need to make benefits understandable (or better understandable)

B – Knowledge of certificates

How much do you agree with the following statements?

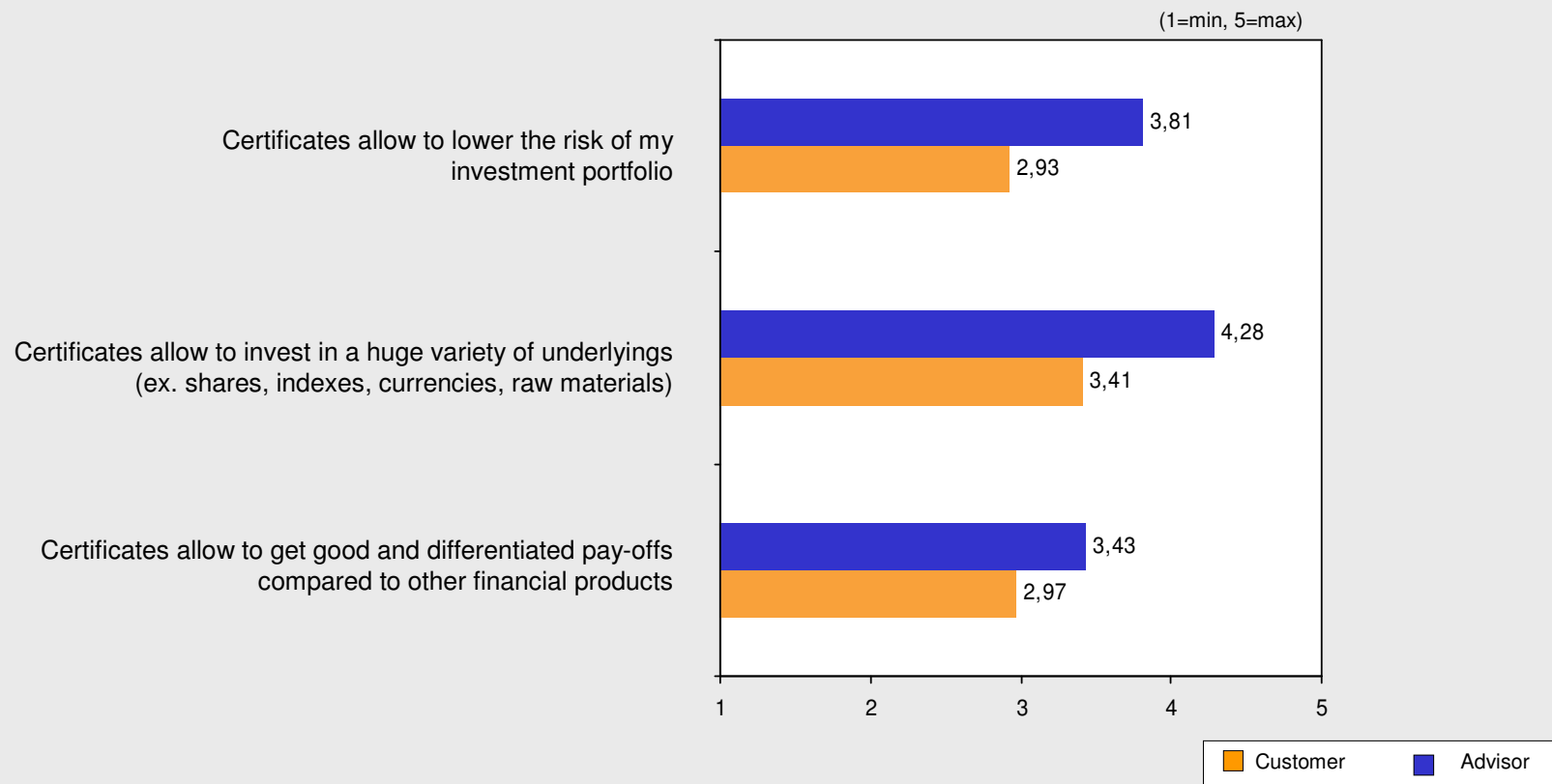


How much do you agree with the following statements?



B – Knowledge of certificates

How much do you agree with the following statements?



B – Knowledge of certificates

- Financial advisors have a better understanding of certificates and a better evaluation of issuers' documentation
- Perception of liquidity/transparency and price fairness is coherent with investors' perception...
- ...while perception of potential benefits is greater for financial advisors than investors-need for increased clarity on specific certificates or standardization?

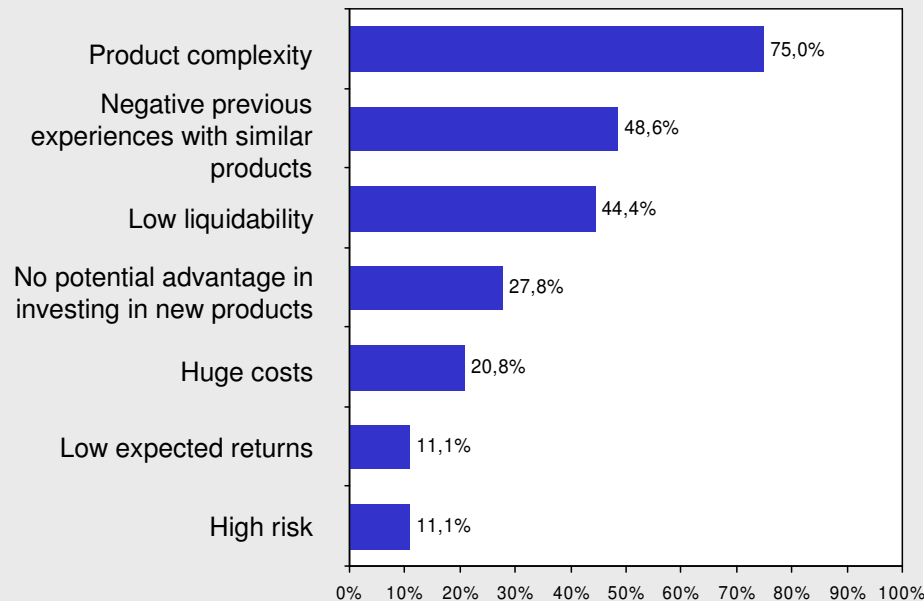
Index

- Section I - Potential Investors
 - Introduction & Sample
 - A – Portfolio structure
 - B – Knowledge of certificates
 - C – Evaluation of some ideal-types
 - D – Comparative perception of investment products

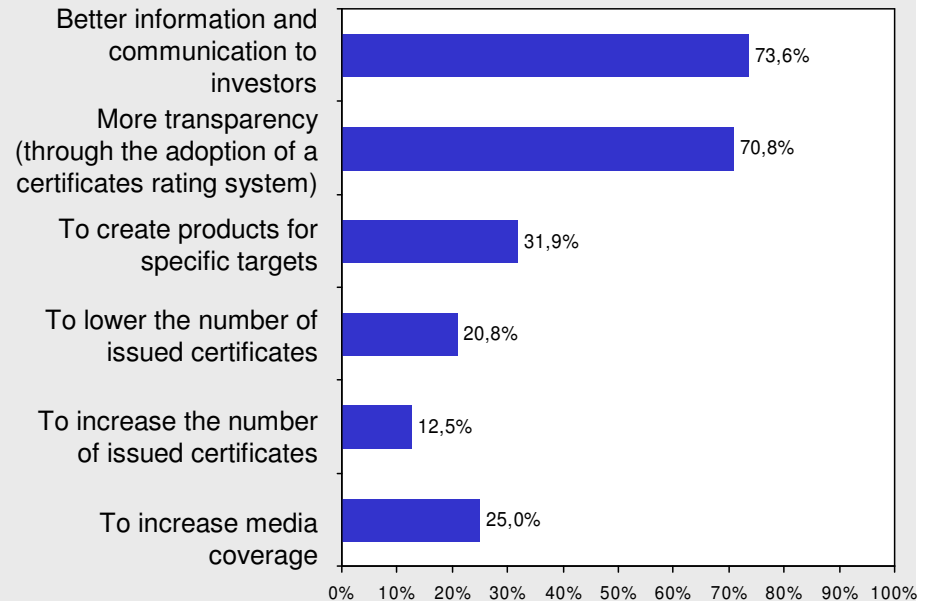
- Section II - Financial advisors and their perceptions of certificates and investors
 - Introduction & Sample
 - A – Consumers' investment preferences (according to financial advisors)
 - B – Information sources
 - **C – Market scenarios according to the advisors' view**

C – Market scenarios

What are the main constraints to the growth of the certificates market?

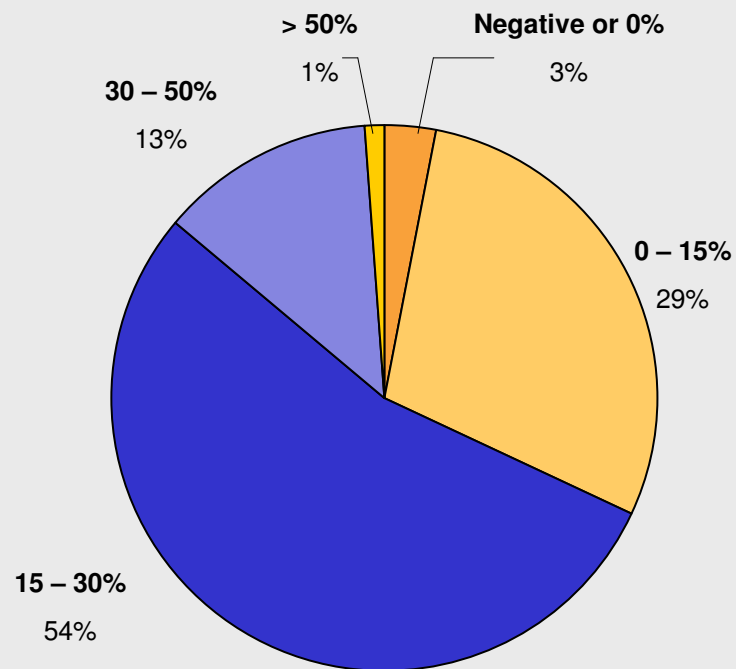


What are the main initiatives that might promote the growth of the certificates market?



C – Market scenarios

What will be the annual growth rate of the market for the 5 next years?



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