LeanVal RESEARCH

Germany needs more equity savers

Ways to strengthen participation in the capital market

Dr. Michael Heise on Global Economics

September 2023

Anyone in Germany who calls for free-market reforms is quickly confronted with accusations of neoliberalism or lobbying. High corporate profits are often not seen as an expression of high competitiveness and efficiency, but rather as a symptom of excessive price demands or job-threatening rationalization. The fact that the success of a market economy and the prosperity of society depends to a large extent on the fact that capital flows into particularly profitable uses is deliberately overlooked by critics of capitalism.

This view changes, however, from the perspective of a shareholder or investor who has a direct stake in the company's earnings. In this role, one is very interested in competitiveness, cost efficiency, and a reasonable strategy of one's own participation. Therefore, a stronger participation in the returns of entrepreneurial success is certainly also a way to improve the acceptance of the market economy.

However, the participation of investors in the capital market is not only to be advocated for this aspect of confidence-building, but it also has tangible economic advantages. A higher level of investor participation improves the financial situation of companies. If there were more shareholders in Germany than the estimated 10 million, companies would have a far greater supply of risk capital for financing growth. There is also the wealth aspect for savers. Private households would achieve a much higher return on assets, which would make assets grow faster and reduce the gaps in old-age provision. Participation in the capital market is therefore of social and economic importance.

In Germany, participation in the capital market is weak. Of the financial assets of private households, around 42% are invested in bank deposits, 27% of gross financial assets are invested in shares and investment funds as well as debt securities, and the remaining 31% are claims on insurance companies and pension institutions.

Germany's deposit ratio is much higher and its investment in securities on the capital market much lower than the average for Western Europe. In the USA, just 13% of financial assets are held in bank accounts, while securities investments account for around 55%. It is therefore no wonder that the return on financial assets in Germany is very low.

Incidentally, this asset structure in Germany also contributes to the fact that inequality in asset development remains relatively high despite all the state support measures for small savers - such as savings allowances, Riester subsidies. The lower income strategy to save, as far as this is possible at all, mainly in bank deposits, while wealthier strategies have much higher share and investment ratios and benefit from the higher returns - or one can say risk premiums - of the capital market.

Time of publication: 13/09/2023 13:00

In the meantime, interest rates on bank deposits have also risen significantly. Although, the current profit yield on shares is around 7%, i.e. significantly higher than the interest rates on deposits, which are still below the inflation rate, i.e. a real consumption of assets. A stronger participation in the capital market is still more attractive from a return point of view than saving, for example, through time deposits. The higher return on shares is based on the risk premium, which compensates for the significant fluctuations over time.

In view of the relatively low participation in capital market returns, wealth accumulation in Germany is based to a particularly large extent on a consumption sacrifice - i.e. very high annual savings. In 2022, private households in Germany will have put aside around 250 billion euros, which is still slightly more than all the other 19-euro countries put together. You can also put it in a striking way like this: Germans work for their money, while others let their money work for them.

It is therefore not surprising that Germany has not really improved in the world ranking of per capita wealth over time, despite high savings efforts; according to last year's Allianz Global Wealth Report, gross financial assets are currently only in 18th place. The per capita gross financial assets (excluding debts) are around 99,000 euros; in the USA they are three times as high and in Switzerland three and a half times as high. But even in a European comparison, seven EU countries plus the United Kingdom rank ahead of Germany in terms of per capita wealth.

The low level of participation in the capital markets also means that a large part of the dividends and share price gains of German DAX companies go to foreign investors, pension funds, direct investors, or fund savers.

The question is how to improve the participation of savers in the capital market and what effects this could have on confidence in free competition and the market economy.

1. Participation in the success of one's own company can be encouraged, for example, through employee shares. It is a good idea of the government to raise the tax allowance for such participation to 5.500 Euros in the Future Security Act. This would make salary conversion much more attractive.

2. It would also make sense to make it easier to save for shares as part of the old-age provision by enabling a tax-subsidized old-age provision deposit account in which investments can be made in shares or other forms of participation. According to the proposals of the focus group on old-age provision of the Ministry of Finance, it would make sense to dispense with guarantees as in the case of the Riester return within the framework of a private-sector solution, since guarantees are not necessary for long-term investments over several decades and severely limit the returns for the saver.

3. Highly regulated forms of investment such as the Riester pension are unlikely to have much effect on the acceptance of market economy processes. Many people tend to use the Riester pension as an opportunity to criticize private-sector solutions, failing to realize that the extremely low interest rate phase brought about by the central banks made it virtually impossible to guarantee the capital required by the Riester system while at the same time taking advantage of opportunities on the capital market.

4. Generation capital, which is intended to stabilize the contribution rates under the first pillar of the old-age provision system, is also a way of making the returns of the capital market available to society. However, since this is a collective capital stock, individuals should not have the immediate impression of participating directly in the returns of the capital market. This effect would be stronger if individualized capital accounts were introduced within the framework of funded pension provision, as is the case with the Swedish model, and the insured were given a choice with regard to the form of investment. It is to be hoped that a further development of generational capital in this direction will be possible.

5. A strengthening of stock market participation in broad sections of the population could also be increased by allowing life insurance companies to invest in shares to a greater extent than is the case today. Here, a stronger participation in the returns of the stock market would be possible due to long lock-in periods. However, these are international regulations within the framework of Solvency II.

If the various opportunities for saving in shares are expanded and the other preconditions are created in the form of financial education and technological innovations, the development will go in the right direction and Germany could also become a country of equity savers. The recent increase in the number of shareholders is encouraging. In particular, surveys among Generation Z (18-24 years) show an increased interest, but also modest expertise with regard to investing in shares. (Surveys DIVA, Union).

The path to strengthening participation in the capital market is certainly not easy. However, it is worthwhile in order to strengthen confidence in the mechanisms of the market economy.

Disclaimer

LeanVal RESEARCH

Notes on investment strategy - Investment recommendation pursuant to § 85 of the German Securities Trading Act (WpHG) in conjunction with the German Securities Trading Act (WpHG). Regulation (EU) No. 596/2014

General

The investment strategy and/or investment recommendations (hereinafter referred to as "analyses") are prepared by LeanVal Research GmbH for information purposes only.

Neither LeanVal Research GmbH nor its employees assume any liability for damages arising from the use of the analyses or their contents or in any other way in connection with them. The analyses do not constitute an offer or invitation to subscribe to or purchase any security, nor do they or the information contained therein form the basis for any contractual or other obligation of any kind. An investment decision should be made on the basis of a duly approved prospectus or information memorandum and in no case on the basis of the analyses. Investors should seek the advice of an investment adviser in making their investment decision. In this respect, the analyses cannot assume an advisory function. The opinions, estimates and forecasts contained in the analyses are solely those of the respective authors. They are date-related, not necessarily the opinion of LeanVal Research GmbH and may change at any time without prior notice.

The information and evaluations ("Information") reproduced here are primarily intended for clients of LeanVal Research GmbH in Germany. Should the original recipient forward the analysis, he/she is obliged to do so in compliance with existing regulations and laws and no obligation of LeanVal Research GmbH towards a third party arises from this. In particular, the information is not intended for clients or other persons domiciled or resident in the United Kingdom, the United States or Canada and may not be passed on to such persons or imported into or distributed in these countries. Distribution of the Analytics in other jurisdictions may be restricted by law and persons into whose possession the Analytics come should inform themselves about and comply with any restrictions. Any failure to comply with these restrictions may constitute a violation of applicable securities laws. Reprinting, redistribution, and publication of the analyses and their contents in whole or in part are permitted only with the prior written consent of LeanVal Research GmbH.

Information sources

All analyses are prepared on the basis of data from a data provider as well as from generally accessible sources ("information") that LeanVal Research GmbH considers to be reliable. However, LeanVal Research GmbH has not verified the accuracy or completeness of the Information and assumes no liability for the accuracy or completeness of the Information. Possible incomplete or incorrect information does not justify any liability of LeanVal Research GmbH for damages of any kind, and LeanVal Research GmbH is not liable for indirect and/or direct damages and/or consequential damages. In particular, LeanVal Research GmbH assumes no liability for statements, plans or other details contained in these analyses with regard to the investigated companies. Although the analyses are compiled with all due care, errors or incompleteness cannot be excluded. LeanVal Research GmbH, its shareholders, corporate bodies and employees assume no liability for the accuracy or completeness of the statements, assessments, recommendations derived from the information contained in the analyses. Data source for all historical prices is Morningstar and LeanVal Research.

Summary of the valuation fundamentals

The valuations underlying the investment recommendations for stocks analyzed by LeanVal Research GmbH are based on generally accepted and widely used methods of fundamental analysis, such as the DCF model, peer group comparisons, NAV valuations and - where possible - a sum-of-the-parts model. The calculated scores (Value, Quality, Stabilty, Growth) are the result of a proprietary model of LeanVal Research GmbH. They result from the comparison of fundamental key figures of the quantitatively analyzed company in relation to comparable companies within a sector (or region). Information on the general approach can be found at www.leanval.investments. The absolute target price and the associated absolute assessment (undervalued, neutrally overvalued) are determined using a forward-looking DCF or ROIC (return on invested capital) method. Estimates of future earnings serve as the basis for this. The earnings estimates are either based on a consensus or are made by LeanVal Research GmbH itself.

Updates

The recipients are not entitled to the publication of updated analyses. LeanVal Research GmbH reserves the right to update analyses without prior notice. A regular update of this document is not intended.

Compliance

LeanVal Research GmbH has taken internal organizational and regulatory precautions to avoid conflicts of interest in the preparation and dissemination of financial analyses. In particular, there are internal information barriers that prevent analysts from accessing insider information. Compliance is monitored by the Compliance Officer.

Explanation of the recommendation system

The relative assessment is based on the various scores of the individual companies in the areas of Value, Quality, Stability, Growth and Momentum which are compared with the average scores of the overall market and/or also with the respective sectors. The companies are ranked on a scale from 0 to 100. From this, the three ratings "unattractive" (0 to 30 on the scale), "neutral" (31 to 70 on the scale) and "attractive" (71 to 100 on the scale) are derived. The relative assessment can change at short notice due to the high complexity of the scores and the multiple interdependencies between the companies analyzed.

LeanVal Research GmbH's rating system for absolute valuation comprises the ratings "undervalued", "fairly valued" and "overvalued". The rating of a share is based on the expected return for the next six to twelve months. The expected return is composed of the prognostic change in the share price and the expected dividend yield. Changes in the discount factor or projected cash flows can lead to significant changes in the target price.

Rating system of the absolute valuation	
Buy	Potential > +15%
Hold	Low upside and downside potential
Sell	Potential < - 15%

Conflicts of interest

In the financial analyses, circumstances or relationships that could give rise to conflicts of interest because they could jeopardize the impartiality - of the employees of LeanVal Research GmbH who prepared the analysis, - of LeanVal Research GmbH as the company responsible for the preparation or of companies affiliated with it, or - of other persons or companies working for LeanVal Research GmbH and contributing to the preparation, must be disclosed. Information on interests or conflicts of interest that must be disclosed exists in particular if

1. significant shareholdings (= shareholding > 5 % of the share capital) exist between the above-mentioned persons or companies and the issuers who are themselves or whose financial instruments are the subject of the financial analysis,
2. the above-mentioned persons or companies manage financial instruments which themselves or their issuers are the subject of the financial analysis on a market by placing buy or sell orders (market making/designated sponsoring),
3. the above-mentioned persons or companies have been involved in the management of a consortium for an issue by way of a public offering of such financial instruments which are themselves or whose issuers are the subject of the financial analysis within the previous twelve months,
4. the above-mentioned persons or companies have been bound by an agreement on services in connection with investment banking transactions with issuers who are themselves or whose financial instruments are the subject of the financial analysis within the previous twelve months or have received a service or a promise of service from such an agreement within this period, insofar as no confidential business information is affected by the disclosure of this information,
5. the above-mentioned persons or companies have entered into an agreement with issuers, who themselves or whose financial instruments are the subject of the financial analysis, for the preparation of the financial analysis,
6. the above-mentioned persons hold management or supervisory board mandates with issuers whose financial instruments are the subject of the financial analysis, or
7. the above-mentioned persons or companies have any other significant financial interests in relation to the issuers whose financial instruments are the subject of the financial analysis.

LeanVal Research GmbH
Bleichstraße 52
60313 Frankfurt am Main
Phone: +49 69 9494 88 050,
Email: research@leanval.investments