The future of advice

A comparison of fee-based and commission-based advice from the perspective of retail clients
Whitepaper

November 2021

Executive Summary

This study looks at the effects of a ban on inducements for the German market. It was prepared by KPMG on behalf of Deutsche Kreditwirtschaft (DK), the German Investment Funds Association (BVI) and the German Derivatives Association (DDV). The study examines the needs of small and medium investors (hereinafter referred to as retail clients). Since they lack experience and sometimes also lack financial education, this client group particularly requires expert support in managing their assets. Often, these investors have to be convinced initially of the necessity of capital accumulation and need an introduction to the capital markets.

Due to persistently low interest rates and demographic change, investing in securities has become an indispensable component of capital accumulation and private pension provision for every citizen. The European legislator has also recognised this and has made the strengthening of private investment one of the most important objectives in the creation of a capital markets union.

The study concludes that the only way of guaranteeing clients appropriate introduction and expert guidance for their securities investments is to maintain commission-based advisory services. A ban on this form of advice would create an advice gap for the group of retail clients who are particularly in need of guidance. This is mainly because fee-based advice does not pay off for these investors with small investment amounts and presents insurmountable cost hurdles. One result of the study is that more than half of all investments made by retail clients are amounts below €5,000 (55.5%) or monthly savings rates of less than €100 (54.6%). Up to an investment amount of €25,000, however, fee-based investment advice is more expensive than commission-based advice; based on the median financial assets of German households in 2017 of €16,900, the cost of fee-based investment advice is 50% higher. However, as German households only hold an average of €6,000 in fund assets, the average costs of fee-based investment advice would in practice be around four times higher than the costs of commission-based advice.

In addition, most retail clients are generally not willing to pay directly for advice. An investor survey conducted for this study revealed that just under 16% of respondents could imagine paying a direct fee for advice. On average, the respondents indicated an appropriate hourly rate of just €34.80. Only 0.3% of respondents would be willing to pay the current average hourly fee of €180. The vast majority (74%) would not be willing to pay a fee for advice at all. This means that, if commission-based advice were to be banned, a considerable number of retail clients would be left with the option of taking less advice or none at all. Since investment advice is essential for the overwhelming majority of investors surveyed (80%), a ban on commission-based advice would in all likelihood lead to these investors – contrary to the declared aim of the European legislator – turning away from the financial markets and no longer buying financial products, or taking the necessarily higher risk of buying without advice. The consequences would be even more drastic for people who have not even considered investing in securities and who, without advisors financed by inducements, would not be made aware of the necessity of this type of investment. This would have extremely negative consequences for retail clients' capital accumulation.

Experiences from the UK and the Netherlands support these predictions. Since the inducement ban came into force in 2013 (UK) and 2014 (Netherlands), the investment advice market has shifted significantly to the detriment of small and medium investors. Minimum investment amounts for taking investment advice are not uncommon in these countries (in the UK, for example, these are often around £50,000). Surveys conducted by the British financial supervisory authority show that the likelihood of receiving investment advice increases significantly with wealth. Smaller investors in particular thus end up without advice. As a result, investors in these two countries put significantly less money in funds than in Germany. This is likely to be related in large part to the aforementioned restrictions in the advisory offering for retail clients.

All this shows that fee-based advice can at best be an (additional) model for wealthy clients, but does not make sense for the average retail client. Moreover, fee-based investment advice is already available to retail clients today but is hardly used by them.

The study also refutes the criticism sometimes heard that commission-based advice is of lower quality and has increased potential for conflicts of interest. Advisors are legally obliged to use the inducements they receive exclusively to enhance the quality of the service provided to the client, and this contradicts the claim of lower-quality advice. Conflicts of interest are a less important factor due to strong regulation, and such conflicts also occur (in a different form) in fee-based advice. Both requirements – concerning inducements and conflicts of interest – are ensured by regular internal monitoring and close financial supervision from authorities.

Table of contents

01 Introduction

1.1 Motivation

In times of demographic change, with the risk of a further decline in pension levels in Germany and low interest rates, it is more important than ever that private investors participate in the capital markets. Strengthening private investment in securities is therefore also one of the explicit objectives in the creation of a single European market for capital (the "capital markets union").[1] Currently, the model of commission-based advice prevails in many European countries, including Germany. It ensures access to qualified, regulated investment advice for all segments of the population – including small and medium investors and residents of rural areas. With this model, net sales of mutual funds in Europe amounted to €3,400 billion in the last ten years alone.[2]

It is sometimes argued that commission-based investment advice is too expensive for clients, untransparent and creates conflicts of interest on the part of the banks. However, this ignores the fact that receiving inducements in commission-based investment advice is only possible in exceptional cases and under "certain strict conditions"[3] (see Chapter 2.1.). Securities services providers have extensively revised and optimised their commission-based advisory processes in recent years. Product and service costs, as well as inducements, are quantified and disclosed in concrete terms. This was also provided for by the legislator, in particular in MiFID II (Markets in Financial Instruments Directive II) and its corresponding implementation in Germany. This ensures comprehensive transparency for investors. (Potential) conflicts of interest are largely avoided, managed or at least disclosed to investors.

Nevertheless, there have been and still are calls for a complete ban on inducements. Work is currently underway on the regular review of MiFID II (the "MiFID review"). One possible scenario is an absolute ban on inducements, in which it would no longer be permissible to accept inducements, even in compliance with the current legislation.

Such a ban could effectively exclude a large part of the German population from investment advice, as alternative forms of advice would not be financially viable for them ("advice gap"). Small investors with low to medium investment amounts and a lack of experience in the capital markets would be particularly affected. Experience from countries such as the UK and the Netherlands, which have already banned inducements, shows that it is precisely this (particularly vulnerable) part of the population that no longer has access to qualified investment advice.

The effects of a lack of investment advice have been examined in various previous studies. Errors in investment decisions cause financial losses for clients[4], and a lack of access to investment advice leads to lower participation in the capital markets.[5] However, a high level of participation in the capital markets is considered economically advisable by the European legislator and is politically desired in the context of the capital markets union.

This study examines the extent to which an absolute ban on inducements would affect the German market for the provision of investment advice and thus how it would affect retail clients. It first outlines the market for investment advice in Germany and analyses the possible impact of an absolute ban on inducements on the supply and demand side. Subsequently, the resulting implications for retail clients are outlined. Finally, the costs of the commission-based investment advice model are compared with fee-based models, and there is an explanation of how inducements bring added value for clients and how potential conflicts of interest are managed.

1 European Commission (2020), p. 7
2 Net sales of UCITS between 2011 and 2020 according to EFAMA Fact Book 2021.
3 BaFin (2018b), p.16
4 Inderst (2014), p. 61 ff.
5 ECB (2011), p. 31.

1.2 Data collection and methodology

Various data sources were used for this study.

In order to find out the clients' view of a possible ban on inducements, the opinion research institute KANTAR surveyed 2,064 people, selected to be representative of the German-speaking population, on their advisory and investment behaviour and their reaction to a possible nationwide introduction of advisory fees.

In addition, the following data were collected from credit institutions of all three pillars of the German banking system (savings banks, cooperative banks and private banks):

- information on the advisory and investment behaviour of retail clients (deposit and transaction volumes) and on the implementation of quality enhancements by means of a survey of 14 credit institutions (for details see Annex 1)

- information on upfront and ongoing fees based on 100 ex ante cost simulations for the most popular retail funds of 11 credit institutions (for details see Annex 2) to compare costs between fee-based and commission-based investment advice

The study also takes into account publications and studies produced by national and European institutions (ESMA, ECB, Financial Conduct Authority (FCA) and Bundesbank) as well as research institutions.[6]

[6] A complete list of the publications used can be found in the bibliography.

02 The investment advisory market for German retail clients

This chapter first introduces the investment advisory models commonly used in Germany. The retail client considered in this study is then defined and their investment and advisory behaviour is described. In addition, the market for investment advice in Germany is outlined and compared with other European markets.

2.1 Differentiation of investment advisory models

Clients in Germany are currently free to choose between commission-based investment advice and fee-based investment advice ("independent fee-based investment advice").

Differentiation by supervisory authority

Investment advisors in Germany can generally be classified into two groups that are subject to supervision by different authorities:

- The Federal Financial Supervisory Authority (BaFin) supervises investment advisors employed by securities services providers and keeps a register of them (employee and complaints register). The legal framework for investment advice provided by financial institutions is regulated at European level in MiFID II and its implementing acts, and at German level in the Securities Trading Act (WpHG).

- Self-employed investment advisors are defined in Section 34 f (financial investment intermediaries) and Section 34 h (financial investment advisors) of the Trade Regulation Act (GewO). They require a licence from the competent chamber of industry and commerce (IHK) or trade authority and, once licensed, are listed in the register of intermediaries and supervised by the IHK. The legal framework for independent investment advisors is set out in the Financial Investment Intermediaries Ordinance (FinVermV).

However, due to the stricter regulations of the WpHG (e.g. obligation to establish a conflict of interest policy, internal control functions and obligation to use inducements for quality enhancements) for securities services providers as well as the inconsistency in how the regionally responsible IHKs or trade authorities supervise self-employed investment advisors, there are large quality differences both between self-employed advisors by region and between self-employed and salaried investment advisors. This section will focus on the legal provisions of the WpHG and salaried advisors.

Commission-based investment advice

Commission-based investment advice is funded in whole or in part by inducements. Inducements are payments from third parties (e.g. the product manufacturer) to the securities services providers. This payment (commission or inducement) is made directly for the conclusion of a transaction, for example in the form of an upfront fee for investment funds.

The term "inducement" is very broad and not exhaustive. Pursuant to Section 70 (2) sentence 1 WpHG, it includes (among other things) commissions, fees and other monetary benefits as well as all non-monetary benefits. The core of the legal provisions is the required quality enhancement for the acceptance and granting of inducements. This means that the acceptance and granting of inducements is permissible (exceptionally) from a regulatory perspective only if three conditions are cumulatively met: 1) the inducements are designed to enhance the quality of the service provided to the client; 2) they do not conflict with the proper provision of the service in the best interests of the client; and 3) the existence, nature and extent of the inducement are disclosed to the client in advance. The German Investment Services Conduct of Business and Organisation Regulation (WpDVerOV) provides specific (non-exhaustive) examples of when an inducement is designed to improve quality (Section 6 (2) WpDVerOV).

The framework for commission-based investment advice has been steadily tightened over the years, most recently with the entry into force of Directive 2014/65/EU (MiFID II), the Delegated Directive 2017/593/EU in 2018 and BaFin's interpretations for German administrative practice (BT 10 of the Minimum Requirements for Compliance (MaComp)). Further clarifications can be found in the regularly updated Q&A of the ESMA for the area of investor protection. In this context, the requirements for receiving and granting inducements (in particular the requirement that the quality of the investment service is enhanced) have been clarified to ensure that any quality enhancement generated by the use of inducements actually benefits the clients. Furthermore, the transparency requirements for inducements have been increased: securities services providers are obliged to disclose all costs and fees to the client prior to a securities transaction (ex-ante cost information). In addition, the client receives once a year a summary of all costs and fees incurred in the previous year (annual or ex post cost information). The client must also be informed in advance of any investment advice that it is not (independent) fee-based investment advice and whether advice is provided on an extensive or limited range of financial instruments.

Fee-based investment advice

On 1 August 2014, the Honoraranlageberatungsgesetz (Fee-Based Investment Advice Act) came into force in Germany, integrating the professional profile of the fee-based advisor into the WpHG and legally defining it.

The law stipulates that fee-based investment advice may only be remunerated by the client. Therefore, fee-based investment advisors may not accept any inducements from providers whose products they broker or advise. If a product is only available to the client with inducements from the provider, these must be paid out to the client. In addition, the fee-based investment advisor must consider a sufficient range of financial instruments offered on the market for their investment recommendations (Section 64 (5) WpHG). In this context, fee-based investment advisors are not only permitted to provide advice but also to broker the acquisition of a specific product.

If a securities services provider provides both commission-based and fee-based investment advice, the two areas must be strictly separated from each other in organisational terms (Section 80 (7) WpHG). This applies to both the personnel and the functional structure of the two areas.

2.2 The retail client segment

MiFID II makes a legal distinction between client segments: retail clients are negatively defined here as non-professional clients (Art. 4 (1) No. 11 MiFID II). For the purpose of this study, however, the client segment is further specified with the term "retail client"; the focus is exclusively on standardised retail banking, i.e. the sale of standard products to clients investing small and medium-sized amounts. Advice to wealthy private clients ("private banking") is not considered, as this client segment is less in need of protection and is not relevant for the EU Commission's goal of increasing retail investor participation in the capital markets.[7]

The German market for investment advice is largely influenced by retail clients. According to Bundesbank figures, the median financial wealth of German households was only €16,900 in 2017.[8] This means that 50% of German households could invest a maximum of €16,900; for 7.5% of households, debt exceeds assets.[9] A further 30% of households had financial assets of between €16,900 and €79,500. However, financial assets also include current accounts and thus funds that are used for everyday consumption or serve as a reserve for unforeseen expenses. In reality, therefore, the investment sums are significantly lower. Due to the high cost of professional investment advice, a standardised solution is the only realistic option for many of these (potential) investors (see Chapter 4.1.).

At the same time, it is important to attract these population groups to investing in the capital markets. On the one hand, it offers significantly better prospects for returns compared with deposits such as call money accounts or savings bonds; another argument is the exceptionally low real estate ownership rate in Germany: just under half of all households own real estate, which is the lowest figure in a European comparison.[10] In the low-interest environment, property owners benefit from rising property prices, unlike tenants. However, tenants can at least partially compensate for this disadvantage by investing in securities, which reduces the divergence between the wealth of property owners and tenants.

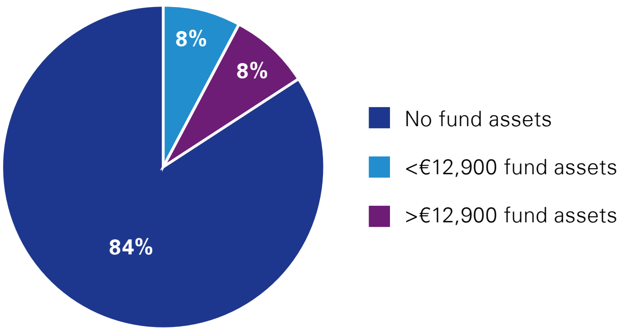
[7] European Commission (2020), p. 7
[8] Bundesbank (2019), p. 34
[9] Bundesbank (2019), p. 27
[10] ECB (2021), p. 7

2.3 Investment and advisory behaviour of retail clients in Germany

Small amounts predominate in the retail client segment

Despite all the advantages, only 16% of German private households held shares in investment funds in 2017.[11] Even if only these households are considered, the median fund assets were only €12,900. This means that 84% of households held no shares in funds at all, 8% held shares worth a maximum of €12,900 and a further 8% held shares worth more than €12,900 (see Figure 1).

Figure 1: Private households in Germany by fund assets



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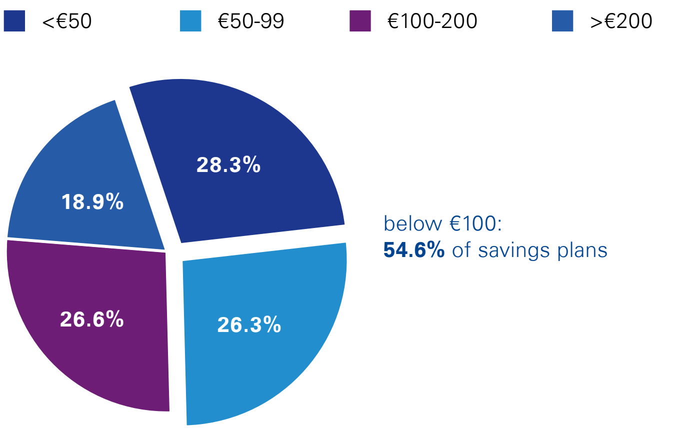
The data collected for this study concerning securities account and transaction volumes at the institutions surveyed confirm these findings and shows that the client structure of the credit institutions selected for this study is representative. The median securities account volume of retail clients at the banks surveyed is €13,100[12] on average, which is just slightly higher than the median fund assets determined by the Bundesbank.

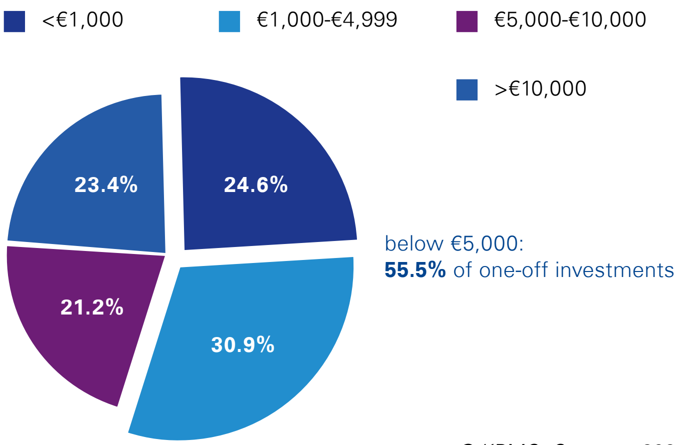
However, it is the analysis of transaction volumes that is particularly interesting for sales activities. The picture is similar: more than half (54.6%) of all securities savings plans involve monthly amounts of less than €100; more than a quarter of all savings plans (28.3%) involve less than €50. Furthermore, more than half (55.5%) of retail clients' one-off investments are less than €5,000 (see Figure 2).

Figure 2: Frequency distribution of (a) monthly savings plan rates and (b) transaction volumes for one-off investments[13]

(a)



(b)



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All this shows that the average retail client can only invest small amounts (e.g. in a securities savings plan) or low one-off investment amounts in securities. For such investors, the costs of fee-based advice are too high in relation to the investment amount (see the detailed comparison in Chapter 4.1.).

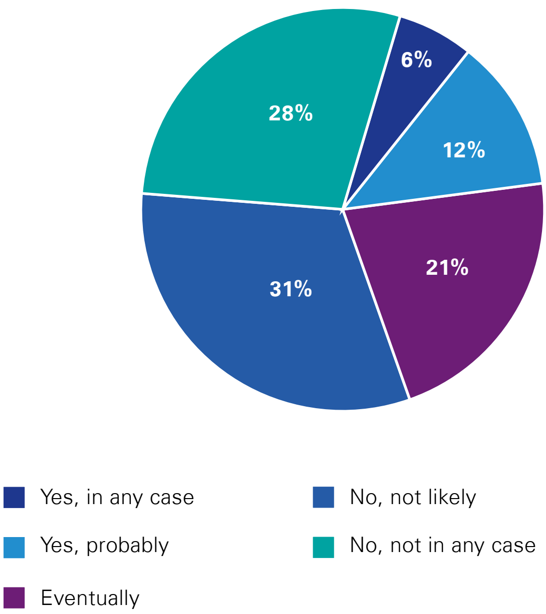
11 Bundesbank (2019), p. 38
12 This figure is derived from a simple average of the median deposit volumes within the institution groups and a subsequent averaging of the group averages.
13 Rounding differences possible.

Qualified investment advice is a prerequisite for capital market participation

According to a YouGov online survey, 36% of the German population over the age of 30 make use of investment advice; moreover, 76% of respondents would like to receive investment advice in the future.[14] According to an analysis of 27,064 securities client data items from 2018, 64% of retail clients regularly take investment advice at their credit institution. The results also indicate that the retail client segment is covered very well by advisory services: for high net-worth clients, the share of clients using advice is not significantly higher, at 77.3%.[15] A comparison of these figures with the distribution of funds and other securities (see first paragraph of this chapter) shows that a large proportion of the advice given does not lead to product purchases. This means that in the commission-based advisory model, many consultations are free of charge.

The European Central Bank stated as far back as 2011 that investment advice was a key factor in households' willingness to invest in (risk-bearing) financial assets.[16] Without advice, German investors would also be likely to invest far less in securities than they have done to date. This is also shown by the current client survey via KANTAR, which indicates that just under a fifth of respondents feel comfortable making investment decisions without advice (cf. Figure 3) and that 28% cannot imagine doing so at all.

Figure 3: Response frequencies to the question "Would you be comfortable making all investment decisions yourself without professional assistance?"[17]



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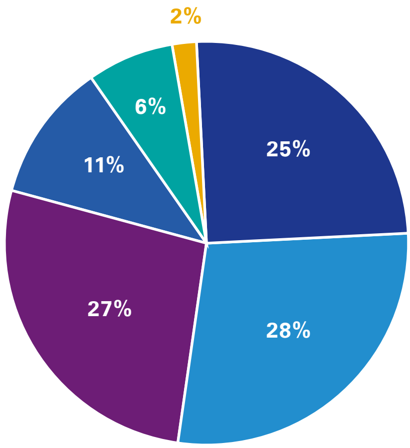
Given the high importance that clients attribute to investment advice, it is hardly surprising that advisory meetings are the most important basis for decisions on investments in securities. A survey conducted as part of a study on retail client decision-making[18] revealed that 80% of investments are made during personal advisory meetings. More than half of the respondents stated that they had largely followed the recommendations of the investment advisor when making their investment decisions.

[14] Concredo (2018), p. 5
[15] Boes (2018), p. 192 f.
[16] ECB (2011)
[17] Data source: Representative study by Kantar (with 2,064 interviews); rounding differences possible.
[18] Chater, Huck, and Inderst (2010), pp. 227, 385.

Personal advice is an important quality feature for clients

German investors still prefer personal interaction when it comes to investment advice: according to the results of the KANTAR survey, 80% of the German population consider personal advice to be "important" to "extremely important" (see Figure 4).

Figure 4: Response frequencies to the question "How important is personal investment advice to you (e.g. at a bank/savings bank branch/office, over the phone or by video)?"[19]



Extremely important	Not so important
Very important	Irrelevant
Important	I am undecided

The YouGov survey[20] provides a similar picture: here, almost nine out of ten respondents stated that they had exclusively or supplementarily used personal forms of advice in their last consultation for a (potential) investment. This would suggest that automated forms of advice such as robo-advice are not an adequate alternative to personal advice, and at best supplement the existing range of advice offered.

[19] Data source: Representative study by Kantar (with 2,064 interviews); rounding differences possible.

[20] Concredo (2018), p. 4.

2.4. The German network of advisors and branches

High branch density

Investors in Germany currently benefit from a dense branch network: compared to other European countries, the number of advisors and branches per inhabitant is very high. With 3.2 bank branches per 10,000 inhabitants in 2019, the branch density in Germany is above the European average (EU 28) (see Figure 5).

This broad branch network is also financed proportionally by inducements – in relation to the investment advice offered in the branches. The positive effect becomes particularly clear when comparing the branch density of Germany with the Netherlands and the UK: in these countries, inducements are prohibited and can therefore not be used (proportionally) to maintain the branch network (see also Sections 3.1. and 3.4.). Consequently, with 0.7 (Netherlands) and 1.1 (UK) bank branches per 10,000 inhabitants, these countries rank at the bottom of the list of larger EU countries in terms of branch density.

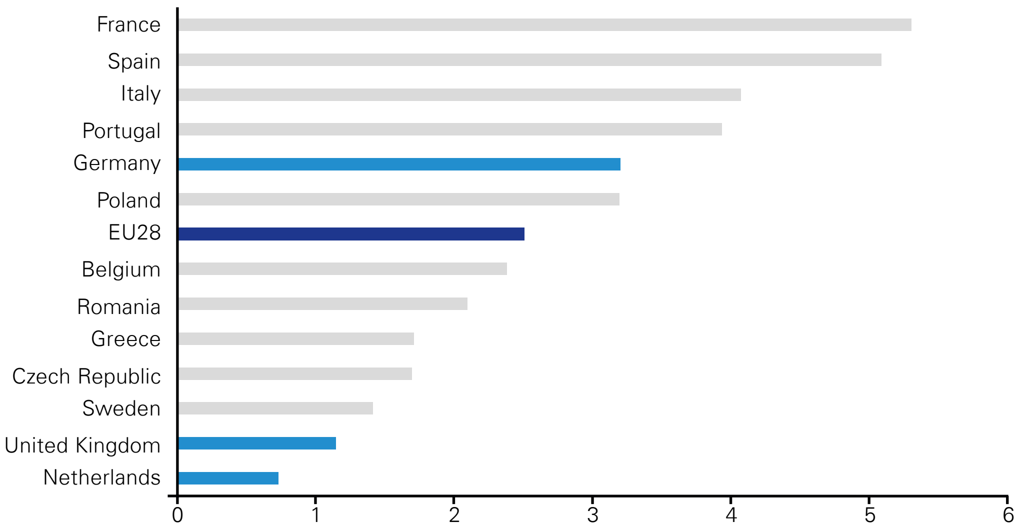
High number of qualified investment advisors

People's access to advisory services is ensured by a high number of qualified investment advisors. A total of 126,185 employees of banks and other securities services institutions provide investment advice (as at 2018)[23]; in addition, there are 38,568 self-employed investment advisors who act as financial investment intermediaries pursuant to Section 34 f GewO, and 228 self-employed investment advisors who provide fee-based investment advice pursuant to Section 34 h GewO.[24] This means that there is one advisor for every 503 inhabitants in Germany.

Here, too, the advice density is high compared to other countries: in the Netherlands[25], there is one advisor for every 671 inhabitants; in the United Kingdom[26], there is one advisor for every 2,439 inhabitants, i.e. for almost five times as many people as in Germany.

In Germany, commission-based investment advice clearly predominates: only 17 financial institutions provide fee-based investment advice. In terms of independent investment advisors, the market share of fee-based investment advice is 0.6%.[27]

Figure 5: Bank branches per 10,000 inhabitants in the largest EU countries[21] in 2019.[22]



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[21] Countries that had more than 10 million inhabitants in 2019 were taken into account. The average (EU28) is given for all EU countries.
[22] Data source: ECB.
[23] BaFin (2018a), p. 43
[24] https://www.dihk.de/de/themen-und-positionen/recht-in-der-wirtschaft/gewerberecht/statistiken-vermittlerverzeichnisse-3344 (as of 2020)
[25] Based on the number of investment advisors according to Adfiz (2020), p. 5.
[26] Based on the number of investment advisors according to https://www.fca.org.uk/data/retail-intermediary-market-2020 (as of 2020).
[27] Investment advisors registered according to Section 34h GewO as percentage of total number of independent investment advisors.

Investment advice market in the UK and the Netherlands – comparable to Germany?

Proponents of an absolute ban on inducements for German securities sales often refer to the regulations in the UK and the Netherlands, which introduced a ban on inducements for the distribution of certain securities in 2013 and 2014, respectively. However, the conditions for a ban on inducements in these two markets were significantly more favourable than in Germany.

The Dutch pension system, for example, is largely based on pension funds, which employers are obliged to offer in most cases; as a result, over 90% of employees in the Netherlands pay into pension funds.[28] For a large proportion of retail clients, this eliminates the need to invest privately in investment funds. This is evidenced by the low share of retail investors in total fund assets, which amounted to 7.4% at the end of 2012 and has since declined slightly to 7.0% at the end of 2020. By comparison, the proportion of retail investors in Germany and the UK is 23.0% and 23.8% respectively.[29] A direct comparison of the remuneration structures with the German investment advisory market is therefore difficult, as the demand for private provision and thus investment advice is significantly lower in the Netherlands.

In the UK, private investor demand for investment funds is comparable to Germany. In both countries, investment advice accounts for around three quarters of sales, with direct sales representing just under 10%.[30] However, the sales structure differs significantly: whereas in Germany just under three-quarters of securities were sold by banks in 2014, merely 1% were sold by banks in the UK, while the market share of investment advisors was 70-75%. In this respect, a system of asset and securities advice provided separately from the principal bank was already established when the ban on inducements was introduced. In Germany, providers and investors would have to adapt much more.

In addition, the UK's financial system has traditionally been more capital market-oriented than in Germany, where banks play a stronger role in financing companies. For example, the London Stock Exchange lists 1647[31] companies, almost four times as many as the Frankfurt Stock Exchange (439)[32].[33] This may reduce scepticism about investing in shares.

Overall, differences in pension systems and sales structures suggest that the negative effects of a ban on inducements would be more pronounced in Germany than in the Netherlands or the UK.

2.5 Conclusion

For a large part of the population, qualified investment advice is a prerequisite for participation in the capital markets and the associated higher investment returns.[34] Germany currently has a very well-developed branch network compared with the rest of Europe. This, in conjunction with the high number of investment advisors, helps Germany to provide its population very good access to investment advisory services geared to its needs.

[28] VB und Opf, p. 11
[29] Data source: ECB
[30] Deloitte (2014), p. 6
[31] https://www.londonstockexchange.com/reports?tab=issuers (as at 31.08.2021)
[32] https://www.deutsche-boerse-cash-market.com/dbcm-de/instrumente-statistiken/statistiken/gelistete-unternehmen (as of at 01.09.2021)
[33] Companies with their headquarters abroad were not taken into account.
[34] ECB (2011), p. 31


option

03 A ban on inducements leads to an advice gap and lower participation in the capital markets

In this chapter, the effects of an absolute ban on inducements are first examined using examples from countries in which a ban on inducements is already in place. It is then shown that in Germany, particularly for clients with lower financial assets, an absolute ban on commission-based investment advice would create a cost hurdle for advisory services that would be difficult to overcome, leading to an advice gap in this client segment.

3.1 Development in other countries following the introduction of a ban on inducements

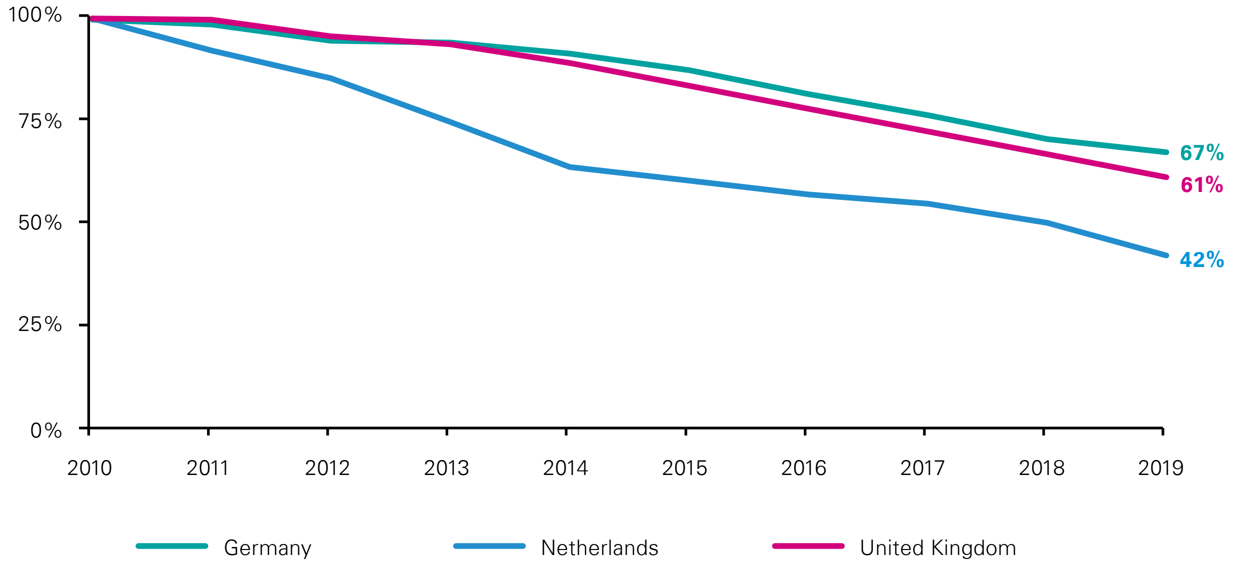
Examples from European countries where an absolute ban on inducements already applies show that the discontinuation of traditional commission-based, in-branch advice for retail clients is not compensated for by alternative models. On the contrary, access to fee-based advice for clients with lower financial assets is extremely limited.

United Kingdom

In 2013, the Retail Distribution Review (RDR) in the UK significantly tightened the requirements for financial advisors. In addition to mandatory disclosure of whether the advice offered covers the entire range of financial instruments ("independent") or only a partial range ("restricted"), a complete ban on inducements from product manufacturers to financial advisors was introduced. As a consequence, the majority of banks have withdrawn from the investment advisory business, which, in conjunction with an increase in the minimum asset requirement for advisory clients, has led to a significant decline in branch density (see Figure 6) and has made access to qualified investment advice more difficult for retail clients.

Since 2013, the pace of branch closures in the UK has increased: while the number of branches per 10,000 inhabitants had been falling by 2% per year until 2013,

Figure 6: Annual development of branch density since 2010[35] (2010: 100%), cumulative



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[35] By considering the period prior to the 2013 and 2014 bans, an anticipatory adjustment of the sales structure by the affected banks is taken into account.

branch density has fallen by an average of almost 7% per year since 2013. In 2019 (1.1 branches per 10,000 inhabitants), branch density was 39% lower than in 2010 (1.9 branches per 10,000 inhabitants).

The number of investment advisors has also fallen significantly in the UK. The largest decline in investment advisors between 2011 and 2014 was in the banking sector, at around 60%; 10% of all investment advisors also changed their status from "independent" to "restricted".[36]

The decline in the number of branches in the United Kingdom – unlike in the Netherlands – is not significantly higher than in Germany, because financial instruments in the United Kingdom were already sold primarily by investment advisors and not by banks before the ban on inducements was enacted (see the remarks on the investment market in the United Kingdom in Chapter 2.4.).

Nevertheless, an advisory gap has emerged in the UK. The size of this gap was calculated by the auditing firm Deloitte on the basis of a YouGov survey, which indicated that 8% of retail clients no longer take investment advice and a further 18% have reduced their frequency of advice or do without investment advice altogether for certain products.[37] It has not yet been possible to compensate for this advisory gap with alternative advisory models: for example, 40% of investment advisory firms have a minimum asset requirement[38], often around £50,000.[39] Even for firms without a formal floor, a data analysis conducted by the Financial Conduct Authority (FCA) shows that advice is taken for high average investment amounts, which indicates extremely limited access to investment advice for retail clients in practice.[40] Complementing this, a 2016 FCA report cites a survey commissioned by the Association of Professional Financial Advisers, which found that 69% of investment advisors surveyed had turned away potential clients in the last 12 months. The most commonly cited reason for this, representing 43% of cases, was that the investment advice would not have been cost-effective due to the client's financial situation.[41]

According to a 2020 study by the FCA, only 17% of consumers with assets of £10,000 or more had used qualified investment advice in the last 12 months, whereas wealthier clients (with assets over £100,000) were significantly more likely to use advice (25% of clients with assets between £100,000 and £250,000 and 38% of clients with assets of more than £250,000).[42] This is further supported by a 2018 consumer survey by market research firm Critical Research.[43]

One factor behind the low demand for advice in lower wealth segments is that – unlike before the ban on inducements – clients are no longer (actively) informed by their bank about the possibility of receiving advice.[44]

Investors with lower assets in particular, for whom there is an undersupply of investment advice services due to the structure of the advice market in the UK, are therefore often referred to automated advice solutions by banks.[45] However, many of these clients say they miss the personal contact with the advisor and are subsequently afraid of making the wrong investment decisions.[46]

Many firms in the UK have no incentive to provide services to less wealthy clients (with typically less complicated client needs) as they are less profitable for them[47]: a single client with £250,000 of assets is more profitable than 10 clients with £25,000 of assets each.[48] The FCA concludes in its 2020 report that while people on high incomes generally have access to advice, people on lower incomes are not as well served by the market and so miss out on opportunities to invest their money in the capital markets for long-term wealth accumulation.[49]

36 Deloitte (2014), p. 8
37 Deloitte (2014), p. 11
38 FCA (2020), p. 39
39 Source: KPMG research on brokerage platforms for independent investment advisors (e.g. https://www.vouchedfor.co.uk/).
40 FCA (2020), p. 33
41 HM Treasury and FCA (2016), p. 6.
42 FCA (2020), p. 10, 12.
43 Ignition House and Critical Research (2018), p. 26.
44 FCA (2020), p. 13.
45 FCA (2020), p. 16 f.
46 FCA (2020), p. 17,18 f.
47 FCA (2020), p. 22.
48 FCA (2020), p. 22.
49 FCA (2020), p. 24.

Netherlands

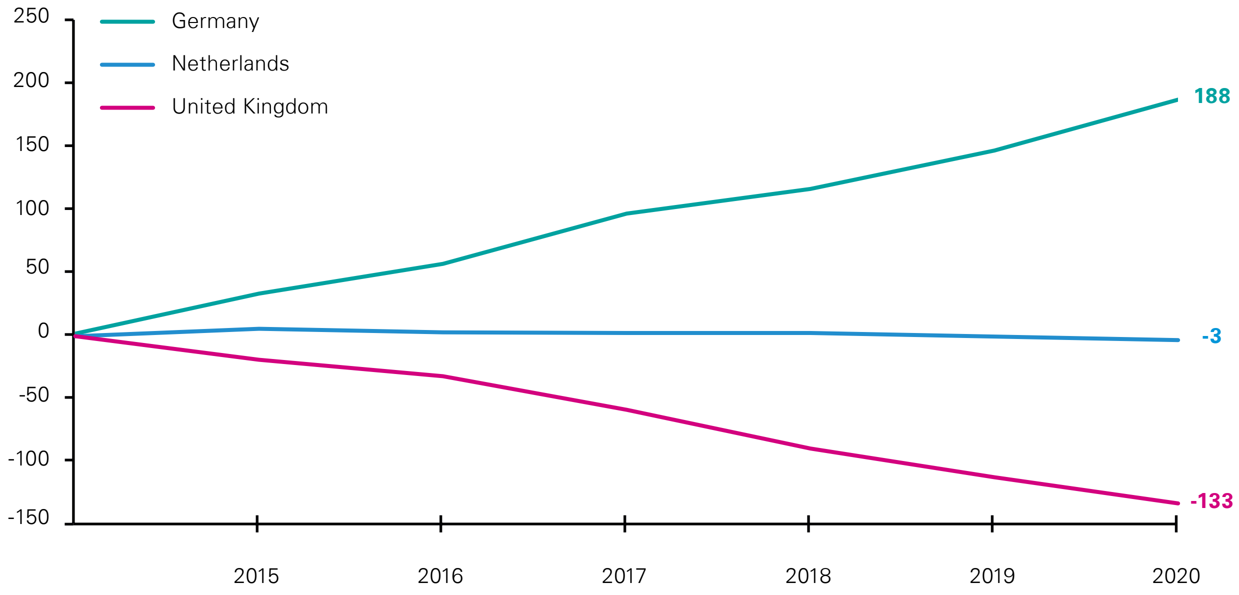
In the Netherlands, an absolute ban on commissions for financial products ("Provisieverbod") was enacted in 2014 after a cap on commission levels introduced in 2009 was judged by the Ministry of Finance to have not had the desired effect. Similar to the UK, there have been widespread branch closures since then: the number of bank branches per 10,000 inhabitants decreased from 1.7 in 2010 to 0.7 in 2019, while in 2020 there were as few as 0.5 branches per 10,000 inhabitants.

For retail clients, alternative wealth management models have since become dominant, but for the most part they do not represent an adequate alternative to personal advice. For example, it has been observed that retail clients largely use execution-only services (i.e. pure execution transactions without advice); in addition, standardised portfolio management solutions are offered, but these often also require minimum investment amounts. Meanwhile, traditional investment advice is now largely a preserve of private banking in the Netherlands and often requires minimum assets of €500,000.[50]

So it is not surprising that the inducement bans in the United Kingdom and the Netherlands have not led to increased participation in the capital markets: Figure 7 shows the net inflows from households into funds since 2014, i.e. during or shortly after the implementation of the inducement bans in the Netherlands and the UK. It can be seen that in Germany, around €200 billion in financial assets has built up via funds within a few years; in the Netherlands, by contrast, wealth accumulation via funds has stagnated during this period. In the United Kingdom, there has even been an outflow of over €130 billion.

This shows that inducements by no means prevent investors from investing in the capital markets; on the contrary, an active advisory approach and good availability of professional investment advice thanks to a

Figure 7: Cumulative net inflow into fund assets since 2014[51]



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[50] DUFAS (2020), p. 3

[51] Data source: ECB. There is no evidence that net inflows in Germany are connected to outflows from other asset classes relevant for wealth accumulation. For insurance products, comparable net inflows can be observed for all three countries; net inflows into equities are stagnating in the Netherlands and the United Kingdom, while significant net inflows can be observed in Germany.

well-developed branch network are catalysts for retail clients to participate in the capital markets. Based on the observations in the Netherlands and the UK, it can be assumed that an absolute ban on inducements in Germany would result in similar developments towards lower capital market participation as well as a drastic thinning out of the branch network and the emergence of an advice gap.

3.2. Clients are not willing to pay for advice

The predicted closure of branches and the considerable decline in the number of advisors in the event of a ban on inducements can be attributed to clients' unwillingness in Germany to pay directly for investment advice. Seventy-four percent of respondents would not be willing to pay a fee for investment advisory services at all (Figure 8). On average, €34.80 was cited as an appropriate hourly rate for financial advice. This is far from common rates in the industry. On average, the hourly rate for fee-based investment advice in Germany is around €180[52] Even the state-subsidised and non-comparable (see Chapter 4.1.) advice provided by the Verbraucherzentrale (consumer advice centre) in Hesse costs investors €80 per hour.[53] The willingness to pay the usual advisory fees for qualified investment advice is vanishingly small: only 0.2% of respondents would be willing to pay between €150 and €200 per hour for investment advice. Only 0.1% of respondents would pay more than €200 per hour. This means that only around 0.3% of respondents are willing to pay the usual hourly rate for fee-based investment advice in Germany.

Many other studies arrive at comparable results: in a study[55] on the acceptance of fee-based investment advice based on data from a German online broker, the majority of clients opted for commission-based advice when both models were offered with a transparent cost structure. To avoid misunderstandings regarding costs, the potential cost differences were explained to the client in advance by the investment advisor on the basis of the client's trading costs over the last twelve months. Even in the group of clients for whom the fee-based model was advantageous from a cost perspective, 27% of clients opted for the commission-based model.

A study for the Dutch mortgage market shows that an advisory fee reduces the willingness to take advice on a new mortgage by a considerable 12%; for refinancing, the figure was as high as 21%. The situation is similar

Figure 8: Response frequencies to the question "How much would you be willing to pay for advice on an hourly rate basis?"[54]

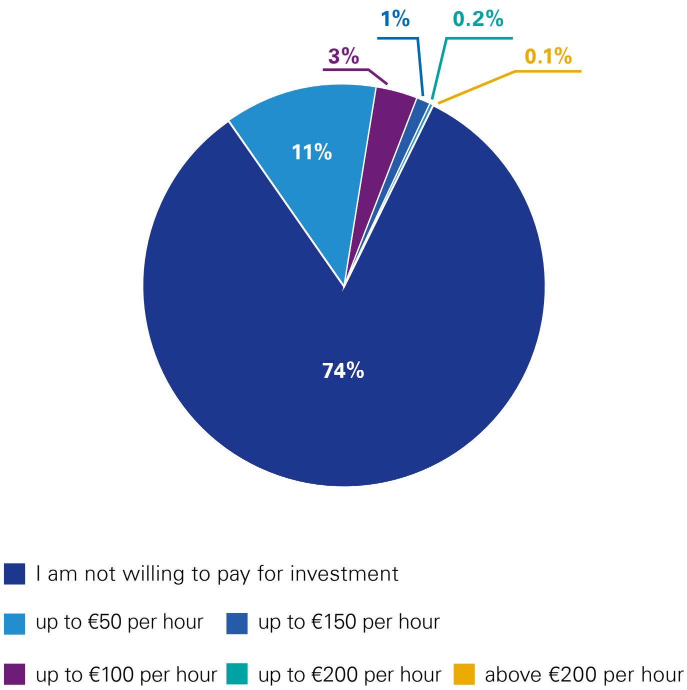

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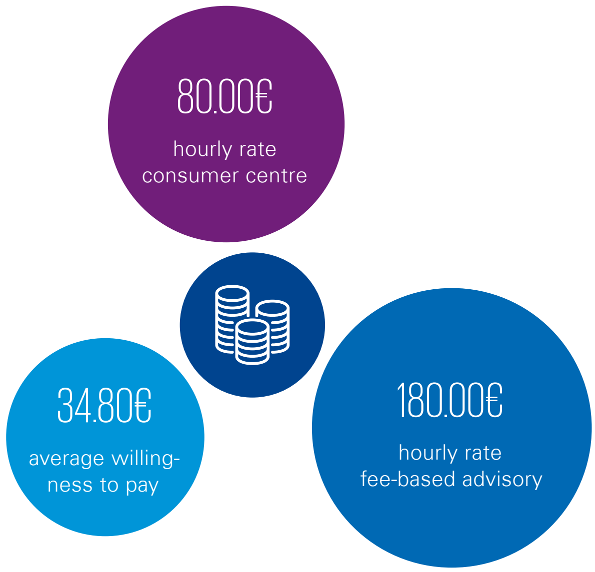
Figure 9: Comparison of willingness to pay for fee-based investment advice with average real hourly rates



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52 See Chapter 4.1.1.

53 https://www.verbraucherzentrale-hessen.de/verbraucherzentrale/preisuebersicht-beratungen-verbraucherzentrale-hessen-30583 (as of 23.09.2021)

54 Data source: Representative study by Kantar (with 2,064 interviews); rounding differences possible; difference to 100%: Don't know / not specified.

55 Meyer and Uhr (2021), p. 25

in the UK: according to the FCA, the majority of respondents to a consumer survey said they would be willing to pay less than 1% of invested assets for advice. On average, respondents are not willing to pay the advisory fees that are customary in the UK, irrespective of the amount invested[56] (see the information box in Section 4.1.).

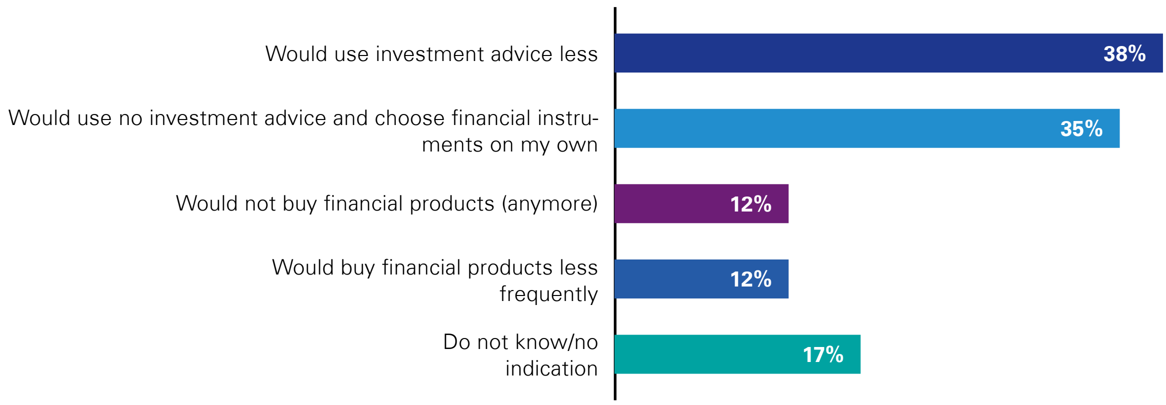
The low willingness to pay a fee for investment advice, even if the costs are the same, can be explained by investors' loss aversion and "mental accounting"[57]: investors weight the certain "loss" of the advisory fee higher than the indirect costs that are deducted from the performance of the recommended product.

Moreover, in the case of commission-based investment advice, the possibility of "free" advice is given (and is also used, see Chapter 2.3.). This is because the costs of the advice are only incurred if the client purchases a financial product; with fee-based investment advice, on the other hand, a fee is always due. This is probably one reason why 85% of respondents in Germany feel that the introduction of an advisory fee is "not fair", according to a 2017 KANTAR survey (see also Section 4.2).[58]

3.3. Reaction of retail clients to the introduction of an advisory fee

The lack of acceptance of advisory fees would have a direct impact on the willingness to provide advice and to invest: KANTAR's customer survey showed that the willingness to both take investment advice and to purchase financial products would decline significantly if a fee were to be charged for advisory meetings in future (see Figure 10). The resulting implications are explained in the following sections.

Figure 10: Response frequencies to the question "How would you react if a fee were charged for every consultation in the future?"[59]



56 FCA (2020), p. 46.
57 Inderst (2014), p. 56 ff.
58 DSGV (2017), p. 11
59 Data source: Representative study by Kantar (with 2,064 interviews); multiple answers possible; rounding differences possible.

3.3.1. Declining willingness to take investment advice

Asked about their reaction to the introduction of an advisory fee, 35% of respondents said they would no longer seek advice and would instead choose financial products themselves, while 38% of respondents said they would seek advice less often.

For investors, this could have a negative impact on the risk-return ratio of their portfolio if they lack capital market knowledge or are overly confident in their own abilities. Inderst (2014) provides an overview of common mistakes that are prevalent among German investors, which notably includes a lack of diversification due to stock picking, overweighting of companies or indices of the home market, and excessive trading activity.[60]

3.3.2. Declining willingness to invest

In addition to the willingness to use investment advice, the introduction of advisory fees would also reduce the willingness to buy financial products. Just under a quarter of respondents said they would buy financial products less frequently (12%) or stop buying them at all (12%) in this case. The correlation between the use of advice and participation in the capital markets is shown by the FCA study from 2020: people who had received "advice and guidance" on investment decisions in the previous twelve months had significantly lower cash holdings than those without assistance (14% vs 49% of investors are invested solely in cash) and a correspondingly higher securities ratio.[61]

The consequences for investors are severe: due to the persistently low interest rate environment, interest rates on savings deposits have been close to zero for quite some time; taking into account the annual inflation rate of between 0.5% and 2% over the past ten years, this means a real loss of wealth. As shown in Figure 11, a retail client with assumed financial assets of €16,900 would have lost around €800 in purchasing power over the last ten years if he had invested the money in savings accounts.

If the same retail client had instead invested his financial assets in the capital markets in line with the portfolio allocation in Chapter 4.1 (cf. Figure 12), his assets would have increased by over €7,000 during this period, adjusted for purchasing power. For many retail clients, the discontinuation of commission-based investment advice would therefore mean a real loss of wealth.

In addition to the serious consequences for the individual investor, the decline in capital market participation misses an important goal of the European Commission's action plan to create a capital markets union, which is intended to build a framework for promoting the investment activities of both retail and institutional investors. The fact that the ban on inducements tends to weaken capital market participation is also shown by the observations for the Dutch and British markets (cf. Figure 7): as already shown in Chapter 3.1, investment funds in these countries have had no significant inflows – or have even recorded outflows – since the inducement ban was introduced.

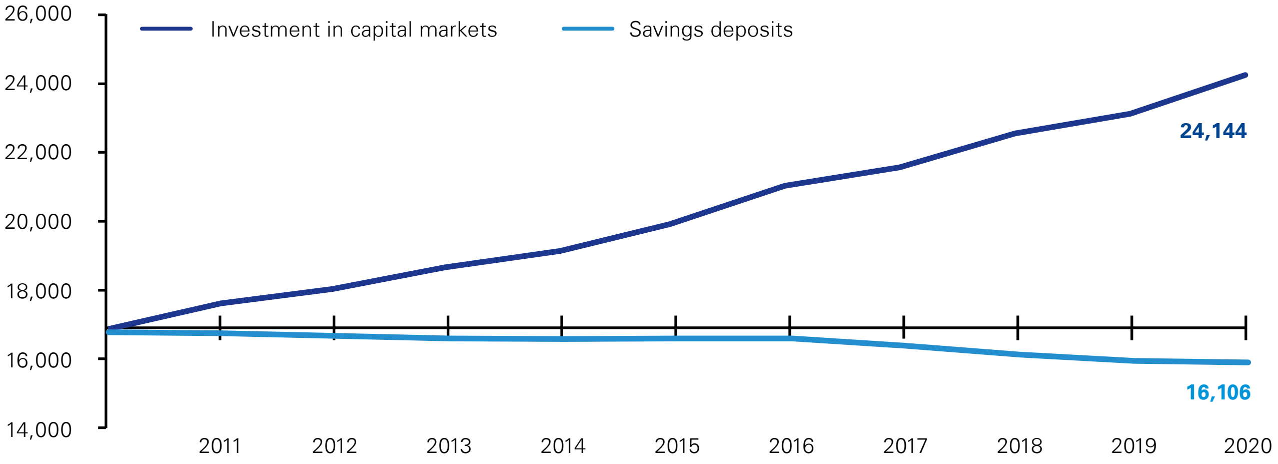
3.4. Other effects

In addition to the above-mentioned reduced willingness or opportunities to take investment advice, an absolute ban on inducements would also restrict access to and availability of advisory services in the medium term.

Due to the low level of customer interest as described in Chapters 3.2. and 3.3., a switch to a fee-based remuneration structure would lead to a significant drop in demand for advisory services. The branch networks of German banks, which are still well developed even in rural areas, are also co-financed by inducements (proportionally in relation to the investment advice offered in the branch). However, it would be difficult to provide on-site investment advice in the branch profitably without inducements. For the client, this would mean significantly impeded access to investment advice.

60 Inderst (2014), p. 62 f.
61 FCA (2020), p. 14

Figure 11: Inflation-adjusted performance of financial assets over the past 10 years when invested on the capital markets[62] or as savings deposits[63]



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In addition, the wealth gaps between wealth groups widen further, as participation in the capital markets becomes less likely, especially for investors with low investable assets. The same is true for people with low financial literacy: in a globally conducted survey on financial literacy[64], a positive correlation between financial literacy and the respondent's likelihood to actively plan for retirement was found in Germany (among other countries). This means that the risk of old-age poverty increases, particularly for population groups with a low level of financial education, if commission-based advice is discontinued.

3.5. Conclusion

Due to the high costs of fee-based investment advice and alternative advisory models, client preference and the likely significant decline in the provision of advice, an absolute ban on inducements would lead to an advice gap that would affect retail investors in particular; as a result, they would have no or only very limited access to qualified investment advice. This is confirmed by observations from the UK and the Netherlands, which have already introduced a ban on inducements.

If an advice gap were to occur as a result of a ban on inducements, this would have serious negative consequences for retail client wealth. The majority of the German population does not feel comfortable making investment decisions without professional advice, while some retail clients would even stop investing in the capital markets altogether as a consequence and accept real wealth losses in the process.

A ban on inducements also reduces the advisory options for clients: it is already possible to take fee-based investment advice, but this is simply not demanded by most retail clients, because they are not willing to pay the hourly rates called for. If, on the other hand, a client is not satisfied with the quality of commission-based investment advice, they have the option to switch to fee-based investment advice. This choice should not be taken away from clients.

[62] Assuming a constant annual portfolio return of 5.30% in accordance with the portfolio allocation used and the return on the assets included according to the BVI fund statistics.

[63] Assuming the average interest rates of three-month, one-year and two-year savings deposits; data source: Bundesbank.

[64] Lusardi and Mitchell (2011), p. 506

04 Direct comparison of commission-based and fee-based investment advice

In this chapter, the core arguments of those supporting an absolute ban on inducements are examined. The following reasons are frequently cited in discussions:

- commission-based advice is uneconomical for the investor
- fee-based advice is of higher quality
- fee-based advice is less prone to potential conflicts of interest

To address these points, a sample calculation is first carried out, which quantitatively underpins the cost differences of the models of advice for retail clients. This is followed by a qualitative analysis and a comparison of the quality of advice and potential conflicts of interest.

4.1. Commission-based advice is more favourable than fee-based advice for the majority of retail clients

In this section, the costs of fee-based advice are compared with the costs of advice under the commission-based model. The general methodology for this is explained in the annex.

4.1.1. Overview

In Germany, retail clients generally have the option to use fee-based investment advice. Due to the relatively small size of the market and the qualitative differences in the advisory services, there are large differences in the hourly rates. According to the Bundesverband unabhängiger Honorarberater gemeinnütziger e.V. (Association of Independent Investment Advisors), the average hourly rate for fee-based investment advice is currently €180 gross[65]; according to the association's fee schedule, an appraisal of existing financial investments including a general discussion of alternatives is €360, which corresponds to a two-hour meeting for initial advice.

Inderst (2014)[66] also indicates a similarly high figure for fee-based investment advice, with an hourly rate of €150; moreover, it is highlighted here that all surveyed investment advisors indicated hourly rates above €100, while some fees were stated at up to €275 per hour. Hourly rates below €100 are only achieved by consumer centres, though these do not offer fully-fledged investment advice, with important features such as specific product recommendations and liability as well as supervision by BaFin not provided. Similar rates were found in an evaluation by Finanztest.[67]

Commission-based advice, on the other hand, initially incurs no direct costs. The advisory costs are financed by inducements, which the bank only collects after the purchase has been concluded in the form of upfront fees and ongoing fees. Clients generally have a personal relationship with their principal bank, which provides the client with holistic support in financial matters. Advisors and clients can evaluate the latter's financial situation together at regular intervals in order to develop suitable investment strategies.

4.1.2. Sample calculation

For the cost comparison, it is therefore assumed that there is a personal relationship including regular exchange between the client and the investment advisor, with the client having one investment consultation per year on average. This corresponds to the frequencies customary in practice (see Annex 1).

65 As at 16.06.2021
66 Inderst (2014), p. 30
67 https://www.test.de/Honorarberatung-Am-besten-unabhaengig-1804931-1804955/ (as of 2009)

Assumed duration of advisory sessions

For an initial discussion, a duration of two hours is taken as a basis (4.1.1). For follow-up meetings, a duration of one hour is assumed. The shorter duration of the follow-up meetings is generally because the initial determination of the client's financial situation and the time-consuming recording of the customer master data are not required. The duration of the follow-up meetings used as a basis for this study corresponds to the results of the survey of credit institutions conducted for this study, which indicate that follow-up meetings last an average of one hour at 85% of the banks surveyed. This does not take into account follow-up meetings that require a new time-consuming determination of the client's financial situation due to fundamental changes (e.g. marriage, inheritance, offspring).[68]

Factors considered for the sample calculation

The costs of advice for the commission-based model are derived from the one-off upfront fee and the ongoing fees for the 78 most frequently sold retail funds in Germany (for the selection and methodology, see Annex 2 and Annex 3 respectively). In addition to the specific product selection, the costs of advice depend on four factors:

1. The investment amount, for which, according to Chapter 2.2, the median financial assets of German households of €16,900 – as the potential "maximum amount" of an investment in securities – are assumed. It is assumed that this amount is already fully invested after the first advisory meeting; since in reality this is usually done gradually (e.g. via savings plans), the calculated costs of commission-based advice are to be understood as a "worst-case scenario".

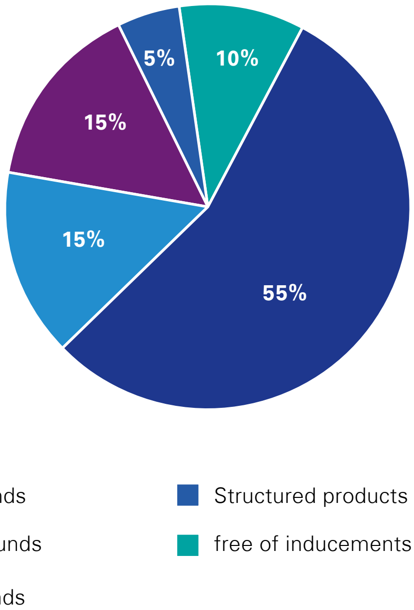
2. The investment horizon (holding period), which is derived from the weighted average holding period of the retail funds most popular with retail investors in Germany (Annex 2). According to BVI investment statistics, this is 6.4 years for equity funds, 9.6 years for mixed funds and 4.0 years for bond funds.[69]

3. The distribution of the investment amount across different product types. This is based on the results of the survey of institutions underlying this study, with those results indicating how frequently the product classes are recommended and this then being used as a proxy for the allocation of funds and non-appropriated products (see Figure 12). By way of background, at the vast majority of the surveyed credit institutions (76.92%), actively managed funds are recommended in more than 75% of the advisory meetings. Exchange-traded index funds (ETFs), equities and bonds, on the other hand, are recommended more selectively in individual advisory meetings. These products do not contribute to the financing of the advisory service but are nevertheless comprehensively recorded in the inventory of the client's financial situation and in individual cases recommended for addition. It is therefore important to also take these products into account in the portfolio allocation as part of the cost calculation, as investment advice is always provided with a view to the client's financial circumstances (income and assets) and thus the overall portfolio. Since the portfolio share of structured products is difficult to approximate via the recommendation frequency due to varied product characteristics (in particular maturity), a survey of the portfolio composition of German households[70] and the market volume of structured products relative to fund products[71] is used instead; on average, this results in a share of structured products of around 5%.

4. The (unknown) performance of the portfolio. The sensitivity analysis in Annex 4 shows that this is only of minor relevance to the overall result for the time horizon considered. It is therefore not included in the following calculation.

[68] For this reason, calculations of the costs incurred for fee-based advice tend to be lower. In fact, the costs for fee-based advice are likely to be higher due to such changes in the client's financial situation. For commission-based advice, on the other hand, no further costs are incurred as a result.
[69] The calculated holding period is derived from the formula 1/((Gross outflows 2020)/(Fund assets end of 2019))
[70] According to Hackethal and Inderst (2015), p. 43, the certificate share is 2.19%.
[71] According to https://www.derivateverband.de/DEU/Statistiken/Marktvolumen, the market volume of structured products was €70.2bn at the end of 2020, corresponding to around 10% of the fund volume held by German households at that time (data source: ECB). Assuming a fund share of 85% in the portfolio, this results in a share of structured products of 8.5%.

Figure 12: Assumed portfolio allocation for the cost comparison



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Results of the sample calculation

The results of the cost comparison for different investment amounts between €5,000 and €50,000 with a constant investment horizon are shown in Figure 13. Here, the costs of the commission-based model are compared with the costs of fee-based investment advice under the assumption that the client holds the assets in their portfolio for 6.5 years in line with the average holding period for mutual funds. The corresponding graph taking into account the performance of the portfolio can be found in Annex 4.

The commission-based model has clear cost advantages over fee-based investment advice for smaller investment amounts; only for investment amounts above €25,000 do the benefits exceed the fees payable. In relation to the typical investment amount of retail clients, the costs of fee-based investment advice are disproportionately high: even the median financial assets, and thus the maximum investable assets for half of all German households, amount to just €16,900; for an investment of this amount, the costs of fee-based advice would be around 50% higher than for commission-based advice. The average fund assets of German households in 2017 were around €6,000.[72] Based on this investment amount, the costs of fee-based investment advice would be around four times higher than the costs of commission-based advice.[73]

The second important aspect is the investment horizon. Figure 14 shows the costs of advice for an investment sum of €16,900 (corresponding to the median financial assets of German households). It is assumed that investments in the same portfolio are made (see Figure 12), but the investment horizon varies between 1 and 10 years. The corresponding graph, taking into account the performance of the portfolio, can be found in Annex 4.

The cost advantages of the commission-based model can also be seen here: while the commission-based model initially incurs higher costs via upfront fees than directly via advisory fees, the investor already benefits financially from the relatively low portfolio commissions in the follow-up consultations after just under 3.5 years. From this point on, the cost savings increase steadily; the longer the investor is invested, the greater the savings.

[72] This value results from the conditional mean value of the fund assets (€37,500) multiplied by the prevalence rate (16%).
[73] If instead the conditional median of fund assets, i.e. excluding households that do not hold fund units, is considered (€12,900), the costs are around twice as high. A comparable result is obtained by comparing the average – conditional – median volume of assets under custody according to the survey conducted in the course of this study (€13,100).

Figure 13: Break-even analysis with a constant investment horizon of 6.5 years

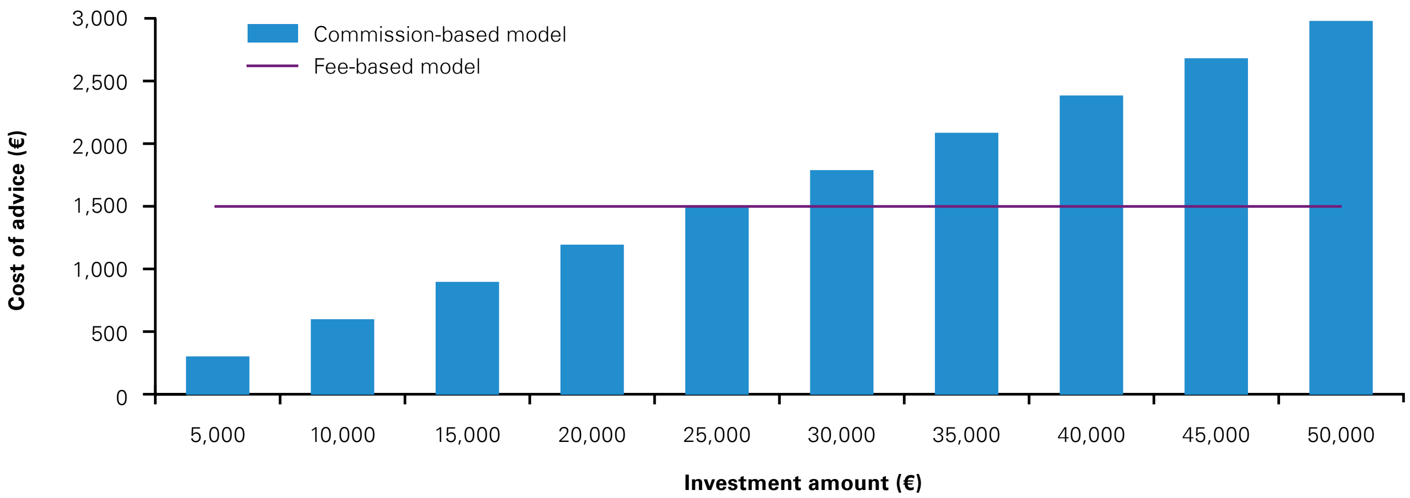

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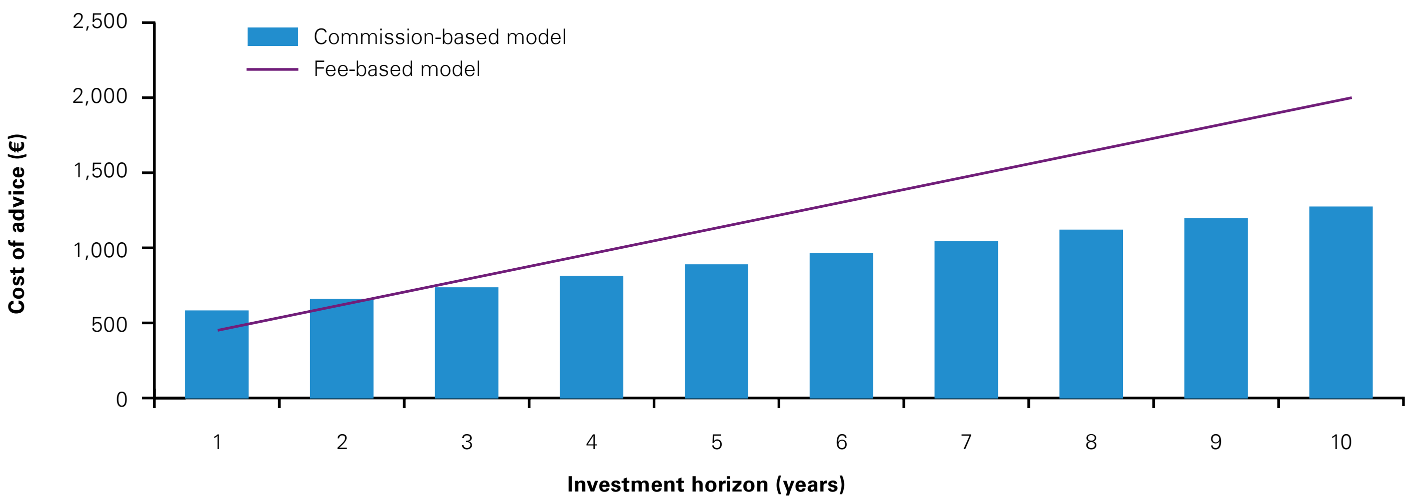
Figure 14: Break-even analysis with a constant investment amount of €16,900



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![lightbulb icon]

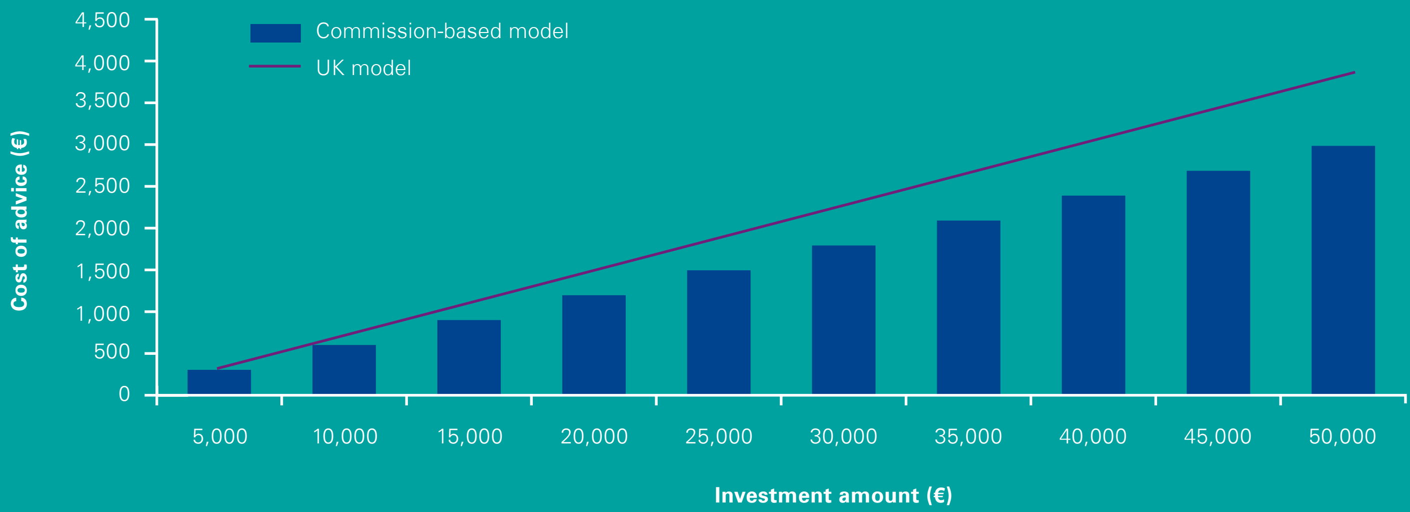
Higher costs also with asset-based remuneration of fee-based investment advice (example of United Kingdom)

Another possible form of remuneration for fee-based investment advice is a fee based on the percentage of assets advised. This form, which is less common in Germany, is widely used in the UK, where around 50% of all advisory services are remunerated by this method.[74] The usual fee is an average of 2.4% for initial advice and 0.8% p.a. for ongoing advice.[75]

Figure 15 compares the costs of the UK model with the costs of commission-based investment advice in Germany. The portfolio allocation corresponds to Figure 12. Here, too, the cost advantages of the commission-based model become apparent, which take effect for small investment amounts and increase further with rising investment amounts.

To summarise, retail clients in the UK have no or extremely limited access to investment advice (usually only above a £50,000 minimum investment amount[76]) – they also pay more on average for investment advice. Interestingly, the FCA's study found that advisory firms generally do not compete on price, despite advocates of fee-based investment advice highlighting the benefits of transparent pricing in this advice model. According to the FCA's study, "Less than a quarter [of advisory firms surveyed] strongly agreed that competitive pricing was key to acquiring and retaining clients."[77]

Figure 15: Cost comparison of the commission-based model with the UK model at a constant investment horizon of 6.5 years



74 FCA (2020), p. 49
75 Average values according to FCA (2020), p. 19
76 Cf. Chapter 3.1.
77 FCA (2020), p. 20

The cost benefits of commission-based investment advice for retail clients depend less on the portfolio allocation, the third important determinant. Figures 16 and 17 show the difference between the costs of advice of the fee-based model and the commission-based model for an equity-heavy and a bond-heavy portfolio allocation, respectively. The cost difference is calculated for all possible combinations of investment horizon and investment amount. Positive values (shown in green) are cost savings, negative values (shown in red) are additional costs of the commission-based advisory model. The usual investment amounts[78] and investment horizons[79] in the retail sector are framed in the two figures.

For example, a retail client who wants to invest €10,000 with an equity share of between 70% and 80% over six years has a cost saving of €647 if they use commission-based advice instead of fee-based investment advice (cf. Figure 16).

This clearly shows that the commission-based advisory model is significantly more favourable in the majority of cases for the usual investment amounts for retail clients, irrespective of the portfolio allocation. If the aim is to achieve a high proportion of bonds in the portfolio (e.g. for retirement planning), the commission-based model is even more favourable for investment amounts between €25,000 and €30,000; however, these are investment amounts that cannot realistically be achieved for the majority of the German population.

Figure 16: Cost differences between the advisory models by investment amount and investment horizon for an equity-heavy portfolio allocation of 0.7/0.05/0.1/0.05/0.1[80]; retail client segment framed

Investment horizon (years) / Investment amount (€)	1	2	3	4	5	6	7	8	9	10
5,000	174	330	486	642	798	954	1,110	1,266	1,422	1,578
10,000	-12	120	252	384	516	647	779	911	1,043	1,175
15,000	-198	-90	18	125	233	341	449	557	665	773
20,000	-384	-300	-217	-133	-49	35	119	203	287	370
25,000	-570	-511	-451	-391	-331	-271	-211	-152	-92	-32
30,000	-757	-721	-685	-649	-613	-578	-542	-506	-470	-434
40,000	-1,129	-1,141	-1,153	-1,166	-1,178	-1,190	-1,202	-1,215	-1,227	-1,239
50,000	-1,501	-1,561	-1,622	1,682-	-1,742	-1,803	-1,863	-1,923	-1,984	-2,044

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Figure 17: Cost differences between advisory models by investment amount and investment horizon for a bond-heavy portfolio allocation of 0.05/0.7/0.1/0.05/0.1; retail client segment framed.

Investment horizon (years) / Investment amount (€)	1	2	3	4	5	6	7	8	9	10
5,000	244	410	576	742	908	1,074	1,240	1,406	1,572	1,738
10,000	128	280	432	584	736	888	1,040	1,192	1,344	1,496
15,000	13	151	288	426	564	702	840	978	1,116	1,254
20,000	-103	21	145	269	392	516	640	764	888	1,012
25,000	-219	-109	1	111	220	330	440	550	660	770
30,000	-335	-239	-143	-47	49	144	240	336	432	528
40,000	-566	-499	-431	-363	-295	-227	-160	-92	-24	44
50,000	-798	-758	-718	-679	-639	-599	-560	-520	-480	-440

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78 Based on the median financial assets in Germany of €16,900.

79 The minimum assumed here is the average holding period of bond funds, which at 4 years have the shortest holding period among the main asset classes considered.

80 Equity funds/bond funds/mixed funds/structured products/products not involving inducements

Conclusion

For a large part of the German population, fee-based investment advice is considerably more expensive than the usual commission-based investment advice. More than half of private households could not even theoretically invest enough to make fee-based investment advice cheaper for them at standard hourly rates. For an average retail client, commission-based investment advice pays off with an investment horizon of around three years for equity-heavy investment strategies, and much sooner for more bond-heavy portfolio allocations.

4.2. Inducements bring added value to clients ("quality enhancement")

In most cases, commission-based investment advice is not only less expensive for the average retail client, it also generates additional free benefits for clients that they would not have if fee-only investment advice were offered.

All inducements that securities service providers accept from third parties – or that they grant to third parties – must by law enhance the quality of the respective service for the client. If it is not possible to enhance the quality of the service by means of the inducements received or granted, these must be returned to the client or may not be accepted in the first place. Non-exhaustive examples of quality enhancements can be found in Section 6 (2) sentence 1 no. 1a) to 1d) WpDVerOV as well as in ESMA's Q&A on MiFID II and MiFIR.[81]

The requirements of European law on the permissibility of inducements have been adopted in Germany largely verbatim in Section 6 (2) WpDVerOV. The examples of additional quality-enhancing services are supplemented in the WpDVerOV by the alternative of improving access to advisory services through a widespread branch advisor network, which ensures the on-site availability of qualified investment advisors for the client, even in rural regions (Section 6 (2) sentence 1 no. 1d) WpDVerOV). The regulatory requirements have the effect that clients benefit from quality-enhancing and additional services in the case of branch-based advice on securities, which could not be maintained in this form if an absolute ban on inducements were to be imposed.

As part of the survey for this study, the institutions were asked to indicate which of the quality enhancements mentioned in Section 6 WpDVerOV and ESMA's Q&A they have implemented. The answers are shown in Figure 18 (Implementation of WpDVerOV measures) and Figure 19 (Implementation of ESMA measures) and explained in the following sections.

Widespread branch advisor network, Section 6 (2) sentence 1 no. 1d) WpDVerOV

One of the most important advantages of the commission-based model for clients is the high bank branch density, which enables nationwide investment advice. For example, 50% of the population in Germany needs a maximum of three minutes to reach a bank branch. Ninety percent of the population can reach the nearest branch in a maximum of eight minutes.[82] The savings banks, the cooperative banking sector and many private banks have a dense branch network. As already shown in Chapter 2.4, this makes Germany one of the top places in Europe. The results of the survey also clearly show that a widespread branch network is considered essential by most banks in Germany; all of the credit institutions surveyed stated that they had such a network.

For customers, this still represents one of the most important quality features: according to the survey conducted by KANTAR, 80% of respondents rate personal advice as important; only 6% said that personal advice was unimportant to them. At the same time, according to a study by Oliver Wyman, the branch is the most important channel for personal advice. In the survey conducted in 2019, 55% of all clients said they preferred branch advice over other channels. In addition, 42% of respondents would switch banks if their regular branch closed.[83] This underlines the importance of a dense branch network for the nationwide provision of advisory services.

The provision of investment advice is not strictly limited to branch opening hours: some of the institutions surveyed stated that they also offer their advisory services outside regular opening hours. In addition, there are offers of advice outside the branch, usually directly at the customer's premises. This is often the only way for clients with limited mobility or limited time resources to receive qualified investment advice and thus to participate in the capital markets.

81 ESMA (2021), p. 111 ff.
82 According to a study by the German Economic Institute (IW).
83 Oliver Wyman (2019), p. 7

Figure 18: Quality enhancement measures implemented by the institutions surveyed in accordance with WpDVerOV

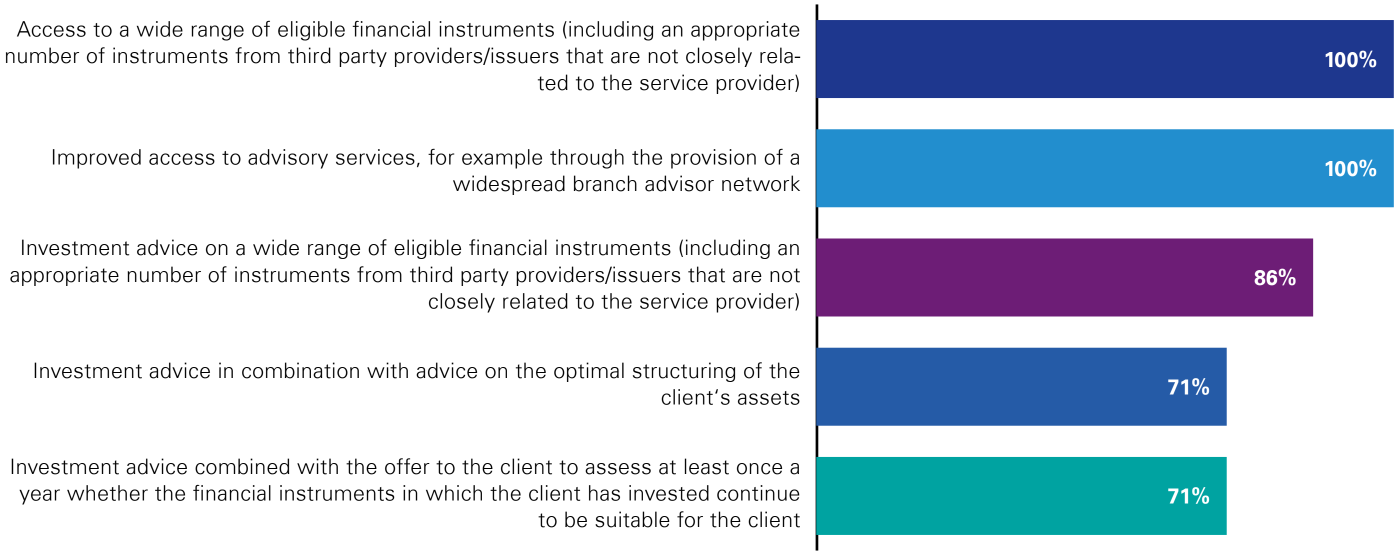

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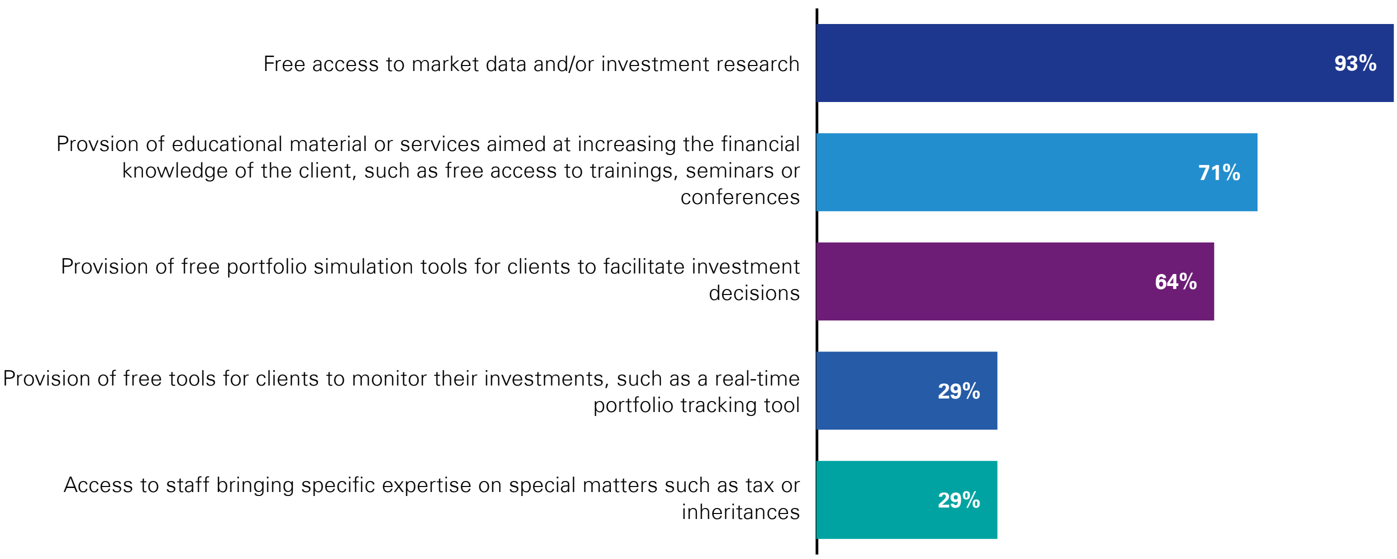
Figure 19: Quality improvement measures implemented by the institutions surveyed in accordance with ESMA Q&A



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Broad range of products and services, Section 6 (2) sentence 1 no. 1 a) and c) WpDVerOV

Another measure to increase service quality for clients is to offer a wide range of products. All of the surveyed institutions stated that their clients have access to a wide range of suitable financial instruments; 86% of the credit institutions also offer these as part of their advisory meetings.

In addition to the products offered, additional services represent an opportunity to enhance the quality of service for customers. For example, 71% of the surveyed institutions stated that, in addition to providing purely product-related investment advice, they also advise clients on optimal asset structuring. Likewise, 71% of the surveyed institutions stated that, in addition to checking the suitability of the recommended financial instrument at the time of the investment advice, they would also (at the client's request) check the client's investment portfolio or the suitability of acquired financial instruments.

In some cases, clients are also offered off-exchange trading with selected partners. This expands the opportunities for clients to trade outside stock exchange hours.

Provision of tools and information material, Section 6 (2) sentence 1 no. 1c) WpDVerOV

In addition to the services already mentioned, many credit institutions offer appropriate tools and access to information material to help clients make decisions and monitor their investments.

For example, 93% of the institutions surveyed offer free access to market data or financial analysis; furthermore, 71% of the institutions provide educational material or services to increase the financial literacy of their clients. Some institutions also offer their clients access to conference calls for investors and analysts. Further analyses of the market and of individual stocks are made available in the form of research papers to enable clients to better assess the current market situation and to improve the basis for forecasts. Other examples of implementation include information on the institutions' websites, information brochures, and presentations and events on various financial topics.

Tools that support clients in making investment decisions are offered by 64% of the institutions surveyed. These include, in particular, self-advice solutions in which clients receive suggestions for suitable financial instruments after entering their existing portfolio. As part of a multi-channel concept, the investment proposals can then be discussed in more detail in a personal consultation by telephone, video chat or in the branch, or executed directly in online banking or via an app. In addition, 29% of the institutions surveyed offer tracking tools that enable customers to monitor their investments in real time.

Another type of tool mentioned in the survey is online calculators, such as performance and investment calculators, as well as inflation, dividend, currency and yield calculators. These enable clients to take a closer look at their finances and develop ideas and discussion points in advance of an advisory meeting. During and after the advice, the client can use these calculators to independently check the development of their investment and the achievement of their investment goals.

Specially trained employees

Inducements also make it possible to conduct advisor training on specific focus topics that go beyond the training required by law. For example, the transformation towards a sustainable financial system also necessitates sustainable direction in terms of investment advice. In addition to complex technical and procedural changes, this also requires advisors who are specially trained in sustainability issues. The client thus benefits from advice on sustainable products that meets the requirements of a sustainable or impact-oriented financial investment if they have a corresponding preference for sustainability. Thanks to comprehensive advice that takes sustainability aspects into account – even before a relevant regulation comes into force – the goal of redirecting capital flows towards sustainable economic activities that has been set by politicians is also significantly supported.

In addition to building ESG capabilities, 29% of the institutions surveyed also said they give their clients access to staff with particular expertise in areas such as tax or inheritance. For clients, this means "one-stop" support on various financial issues. Lower-income client groups in particular benefit from this, as they do not have to pay an additional fee for advice on these topics.

Conclusion

Clients benefit from services that go beyond pure product advice, because banks use the inducements received from commission-based investment advice to enhance the quality of their investment advice. The majority of banks offer advice on asset structuring in addition to advice on a wide range of financial instruments; in some cases, advice on dealing with taxes or inheritances is also part of the service portfolio. To complement the advisory service, many banks provide their clients with tools that support them in their decision-making. Most banks also provide their clients with opportunities for independent financial education – for example, through information materials on websites accessible to their customers – and thus make an important contribution to increasing the general financial literacy of the population.

Furthermore, inducements enable banks to offer their advisory services nationwide and thus make an important contribution to promoting the securities culture as well as indirectly supporting the regional economy in Germany. The combination of high branch density and specially trained advisors can help significantly to achieve the EU action plan objectives to reorient capital flows towards a sustainable economy. Demand for personal advice remains high and can only be met by the dense branch network.

4.3. Conflict of interest potential is not limited to commission-based advice

Potential conflicts of interest can never be completely ruled out – this applies equally to the commission-based and fee-based model. The following section provides an overview of potential conflicts of interest inherent in advisory situations. First, conflicts of interest in commission-based advice and measures introduced by banks to mitigate these conflicts of interest are analysed. These are then contrasted with conflicts of interest that can arise especially in fee-based models.

4.3.1. Commission-based advice

Commission-based investment advice involves no direct costs, as the securities services company providing the investment advice is at least partially remunerated by inducements from the providers or issuers of the financial instruments. The amount of the remuneration is negotiated individually between the product manufacturer (usually investment companies) and the advisory service provider (usually branch banks) and varies depending on the financial product for which the advisory service is provided.

This can potentially create a conflict of interest: if two products exist with different levels of inducements, the bank may have an incentive to recommend the product with the higher inducements to a client. The following section describes how potential conflicts of interest are mitigated by securities service providers.

Managing potential conflicts of interest

The lawful handling of potential conflicts of interest is ensured by extensive legislation and by the banks' interest in long-term customer loyalty.

The European legislator has established regulations for the avoidance and handling of conflicts of interest at the European level in MiFID II. In order to prevent conflicts of interest, institutions must meet extensive requirements with regard to remuneration policy, corporate organisation and product governance. At the national level, MiFID II is implemented within the framework of the German Securities Trading Act (WpHG); according to Section 80 (1) no. 2 WpHG, institutions must take permanently effective precautions for appropriate measures to deal with conflicts of interest.

In order to avoid and minimise conflicts of interest, various measures have been implemented to make the investment advice process more objective. For example, objective product selection and review processes ensure that the amount of the inducements is not a selection criterion for advisors. In addition, as a result of the equivalence check, lower-cost alternatives are recommended in preference to higher-cost offers, even in the context of investment advice, if they are equally suitable for the client. The quality of advice and objectivity is also enhanced by system support, e.g. through model portfolios. This also helps to reduce individual errors made by the investment advisor. The effectiveness of the measures taken is ensured by processes for auditing sales activities.

The legally prescribed conflict of interest policies ensure that any conflicts of interest that could not be avoided by these extensive measures are dealt with properly. Among other things, these policies must identify potential conflicts of interest between advisors and clients and define measures for their organisational handling.

Banks' interest in long-term client loyalty prevails

It is also in the banks' interest to ensure long-term client loyalty. Banks want to go beyond investment advice and to provide other services, such as custody account management and lending.

A solid foundation of trust and a high level of client satisfaction are important for long-term client loyalty and these are closely linked to the client's financial performance, meaning that it is in the bank's own interest to help the client achieve this. It is therefore not in the bank's long-term interest to offer the client products with high premiums based on the prospect of short-term and one-off higher profits without a positive outlook for the client's performance. Ongoing fees also align sales and clients interests, as part of the remuneration is only paid downstream.

Systematic deficiencies in the investment advisory processes and an associated accumulation of cases of incorrect advice, as well as permanently weak performance for clients' investments, would lead to reputational damage for the bank, a breakdown of the client relationship and difficulties in acquiring new clients. Here, too, it is quite clear that the bank's long-term interest in providing advice in the economic interest of its clients clearly outweighs its interest in short-term monetary gains. That inducements are not a significant driver of potential client dissatisfaction is shown by an evaluation of complaints from the institutions surveyed in this study: less than 1% of all complaints registered by the institutions within the last three years were related to inducements.

4.3.2. Fee-based advice

Fee-based advice is legally regulated by the WpHG. Pursuant to Section 64 (5) no. 2 WpHG, (independent) fee-based advice may only be paid for by the client; inducements may therefore not be used to finance the advisory service. This is intended to avoid conflicts of interest.

However, fee-based investment advice is by no means free of conflicts of interest; these are of varying nature and require individual analysis according to the respective form of remuneration. Basically, there are three common forms of remuneration for fee-based investment advice:

- flat fee
- hourly fee
- percentage fee depending on the advised assets

For all three forms of remuneration, the fee amount is not dependent on product sales.

Over- and under-advising

In the case of flat or hourly remuneration, there is an interest on the part of the advisor in providing advice as frequently as possible, as the remuneration is directly dependent on the frequency of advice. This can lead, for example, to a focus on recommending complex products or asset structures, which can cause increased effort in explaining, monitoring and evaluating the investments ("over-advising"). In the case of hourly-based remuneration, the advisor also has an interest in advice lasting as long as possible.

Studies from the UK confirm this, where more than 90% of new clients are advised through "ongoing services" instead of "one-off services". Even if clients are free in principle to receive either one-off or ongoing services, there is a justified fear that new clients will be advised specifically – the "default option" – through services with ongoing advice. Such clients may therefore pay for services they do not need at all.[84]

If the advisory fee is based on a percentage of the assets advised or if a regular – e.g. monthly – fixed fee is paid as part of a continuing advisory relationship, the advisor has an interest in providing advice as infrequently as possible and with as little effort as possible, as the fee is not dependent on the frequency of advice; in contrast to flat or hourly-based fees, this can therefore lead to "under-advising". Such an advisory model is likely to be available only to wealthier clients because the fee-based advisor earns comparatively less from clients with lower assets.

[84] FCA (2020), p. 19 f.

Lack of cost transparency

Only when a flat fee is agreed are the costs transparent for the investor. This is not the case for the other two remuneration models, remuneration per hour advised and remuneration per assets advised.

At the beginning of the advice, it is not clear to the investor how much time the specific advice will take and how many follow-up appointments may be necessary. The investor knows the hourly rate but not the total fee. In some cases, problem areas and the resulting need for special advice only become apparent in the course of the consultation. These circumstances remain unclear, especially for the inexperienced investor, and the resulting need for advice cannot be estimated.

Experience from the UK shows that the sellers' interest in turnover leads to high costs for the investor. The UK financial regulator notes that there are signs of poorly functioning price competition, as customers attach importance to high service quality but not to low prices. Providers exploit this situation to their advantage.[85] It can also be seen that clients in the UK often have no clear idea of what their advice costs. They base the quality of advice primarily on the performance of their portfolio. This shows that one of the arguments against commission-based advice – that fee-based advice is always more transparent for clients and would thus increase cost competition and minimise conflicts of interest – lacks substance.[86]

Focus on meeting client expectations

Clients pay the advisory fee in the expectation of concrete recommendations for action (usually in the form of product recommendations). Depending on the client's financial situation, there are two options: a specific action or product recommendation, and a "hold" recommendation if there is no need for action.

It stands to reason that clients are more satisfied with a specific recommendation, because otherwise the feeling could arise that the advisor "has not really done anything". In this respect, fee-based advisors might be inclined to recommend products more frequently even though there is no need for action. There is thus a potential conflict of interest between the advisor's interest in fulfilling client expectations and the client's interest in optimal asset structuring.[87]

Interest in high advised asset amounts

If advisor remuneration depends solely on the amount of assets advised, there is also an interest on the part of the advisor in acquiring clients with the highest possible assets. However, in addition to the obvious advantages of this form of remuneration due to "profit sharing" through asset growth in the event of advantageous product recommendations by the advisor, potential negative implications must also be taken into account: in some situations, alternative courses of action that reduce the amount of assets advised are in the client's best interest. This could be, for example, early loan repayment or taking advantage of the exemption limit for cash gifts to family members. For the advisor, the interest here would be to advise against this in view of the potential reduction in income.

4.3.3. Conclusion

Conflicts of interest can arise in both advisory models, regardless of the form of advisor remuneration. It is therefore of great importance to identify potential conflicts of interest and to take appropriate measures to detect, avoid and deal with them.

In the case of commission-based investment advice, German banks have implemented effective measures and processes to prevent conflicts of interest as part of the extensive regulatory requirements in this area; for example, potential conflicts of interest are identified as part of the prescribed conflict of interest policies and mitigation measures are defined. Transparency with regard to inducements as part of ex ante cost information and the distinction between independent and non-independent investment advice also helps to ensure that clients are aware of potential conflicts of interest and can evaluate product recommendations accordingly.

Conflicts of interest also arise in fee-based investment advice, but these have not yet been regulated and are therefore often not apparent to the client. A ban on commission-based advice therefore by no means eliminates all potential conflicts of interest in advisory relationships; they merely occur in a modified form in the remaining forms of advice and would therefore also have to be addressed accordingly in future.

85 FCA (2020), p. 20
86 FCA (2020), p. 20
87 See also Roßbach (2011), p. 271 and Frisch (2015), pp. 246, 250.

05 Summary

This study shows that an absolute ban on inducements would have a negative impact on the provision of advisory services to clients and clients' use of these services: clients attribute importance to personal advice. At the same time, however, they are not willing to pay advisory fees because the "certain loss" from the advisory fee acts as a deterrent. In fact, fee-based advice also involves disproportionately high costs for a large part of the population in Germany; for the average retail client, it is 50% more expensive than comparable commission-based advice. As a reaction to the introduction of an advisory fee, many clients would therefore no longer seek investment advice and/or invest less frequently or not at all in the capital markets. In addition, the discontinuation of income from inducements would result in a decline in branch density.

Overall, therefore, inducements do not discourage investors from investing in the capital markets. On the contrary, an absolute ban on inducements would reduce retail client participation in the capital markets. This assumption is supported by observations from the Netherlands and the UK, where inflows into funds have stagnated or declined since the introduction of the ban on inducements, while Germany has seen high levels of new investment by households over the same period.

The study also shows that, due to the obligation to use inducements for quality enhancement measures, commission-based advisory services improve the advisory service and offer great added value for clients; for example, inducements enable the provision of additional information material, specially trained staff or tools.

Potential conflicts of interest, on the other hand, exist in both advisory models. In the case of commission-based advice, these are subject to strict regulation and therefore only play a minor role. In contrast, effective regulation of conflicts of interest for fee-based advice is still to be introduced.

The study concludes that an absolute ban on inducements would not only lead to an advice gap for retail clients and a decline in private pension provision, but would also go against the objectives of the capital markets union at European level.

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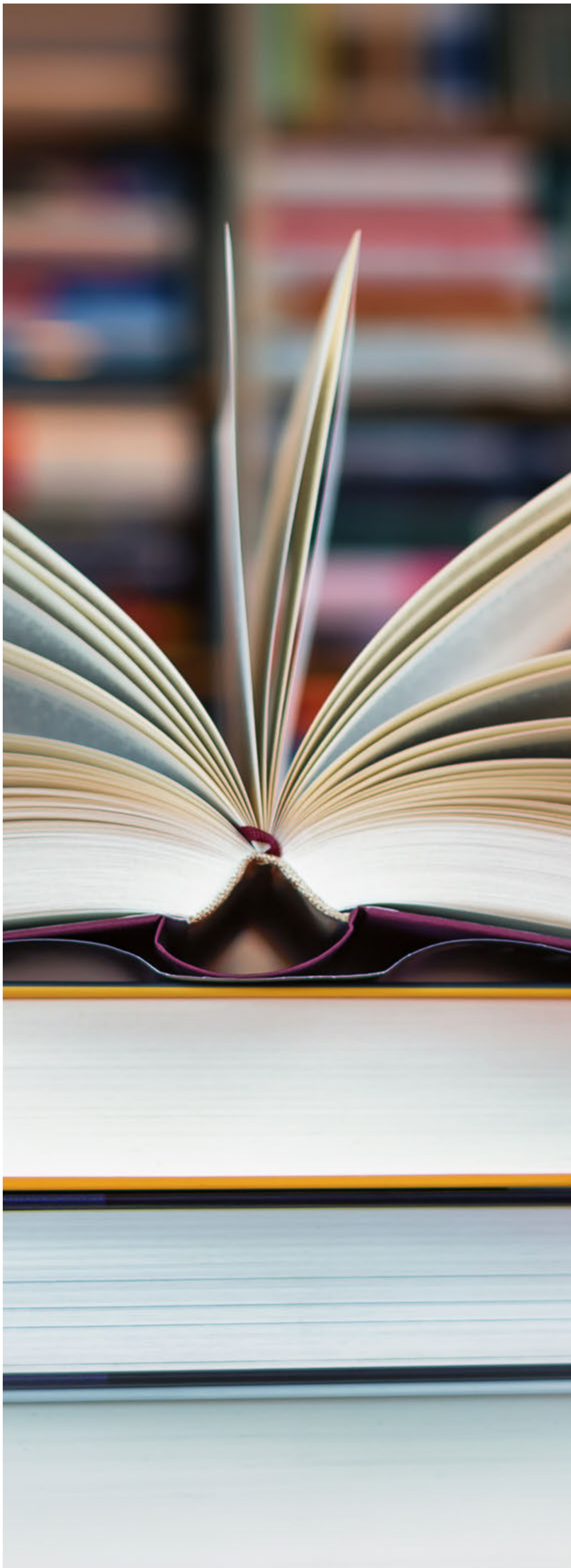


07 Annex

Annex 1: Questionnaire on investment and advisory behaviour and quality enhancements
The purpose of looking at the advisory and investment behaviour of retail clients is to classify how these clients are "set up" financially and what expectations they have of investment advice.

The advisory and investment behaviour of retail clients was surveyed by means of a questionnaire in which the participating 14 institutions were asked to indicate the average deposit volumes and to classify the average transaction volumes of retail clients for one-off investments or savings plans into predefined categories. For the savings bank sector and the cooperative financial group, these data were collected by the respective central depository. Private sector institutions were surveyed directly. Overall, the sample collected covers 11.96 million securities accounts (46% of all retail securities accounts in Germany[88]).

Furthermore, the institutions were asked about the number of advisory meetings per year and the number of individual advisory clients for the period between 2018 and 2020, as well as the duration of an average advisory meeting. In addition, the institutions were asked to rank the frequency of recommendations of different product classes[89] during an advisory meeting. The results of this were used to create portfolio allocations for the cost comparison.

As part of the questionnaire, the institutions were also asked about the implementation of the legal requirements for enhancing service quality for retail clients. In particular, the standard examples pursuant to Section 6 (2) sentence 1 WpDVerOV as well as the recommendations of ESMA for additional or higher-quality services in the context of inducements were queried via multiple-choice questions. Further measures of the institutions could be entered in free text fields. In addition, the number and type of complaints in the period between 2018 and 2020 were queried as an indication of customer perception of the service offered.

In addition, a survey was conducted by KANTAR by asking clients direct questions about their investment behaviour. These included questions on the importance of personal advice and the willingness to pay an advisory fee for advisory services.

Annex 2: Data collection for upfront and ongoing fees
Data on upfront and ongoing fees were collected to enable a cost comparison between commission-based and fee-based investment advice.

As the sample was compiled, the aim was to achieve the broadest possible market coverage. In addition to the largest private-sector banks, cooperative banks and savings banks of various sizes were surveyed, thus covering the three pillars of the German banking system.

In total, data were collected from eleven institutes:

– three private commercial banks

– three cooperative banks

– four savings banks and DekaBank

All participating institutions were asked to provide ex ante cost simulations[90] for the three financial products[91] most frequently recommended in the retail client segment in the product classes of equity, bond and mixed funds.

[88] Data sourceBundesbank
[89] The product classes queried include funds, ETFs, equities, bonds and certificates.
[90] Each based on €5,000 (one-off investment) and €100 (conclusion of savings plan) investment amount, execution venue off-exchange; data collection period: 11.05.2021 – 10.06.2021
[91] If the recommendation frequency could not be determined by the bank, the gross sales are used as an approximation

ETFs were excluded from the data collection, as they are not relevant for inducements. Since no standardised special conditions are agreed in the retail business, the conditions of the ex ante cost statements were used, which show the standard rate (usually the maximum) of the upfront and ongoing fees in the form of inducements from the ongoing product and service costs for the respective institution. In this way, a total of 100 ex ante simulations were collected for 78 funds.

A comparison with the total inflows to all mutual funds shows the high relevance of the 78 products analysed. They reported net inflows of €17.71bn for 2020, compared with €19.40bn for mutual funds in total. This means that the sample accounted for 91.28% of total net inflow. However, it should be noted that net inflows can also be negative.[92]

No differentiation by fund domicile was made in the data collection, as the approach of surveying the most frequently recommended products results in a sufficiently representative sample in terms of fund provenance.

The costs of structured products were requested from DDV issuers with a market coverage of 96% of the volume collected by DDV. The cost data is based only on products that are sold in the retail advisory business. The average costs were then calculated on a volume-weighted basis.[93]

Annex 3: Comparison of cost of advice

This section explains the data model for the cost comparison in the context of this study. The calculation of the cost of advice of the two models is first explained, in order to then outline the procedure for carrying out the cost comparison by means of a break-even analysis.

The individual cost components (in percent) of the funds in the data collected are first aggregated by product class. The costs are weighted according to the net fund assets in Germany as per the BVI investment statistics as of 31 December 2020. Funds not covered by the statistics are weighted using an approximate value. This is done using the total net fund assets of the respective fund according to Morningstar, from which the fund assets in Germany are then calculated approximately using the share of fund assets held by German investors in total European fund assets (EU 27 and the UK).[94] The weighting is carried out separately for each fund class. In the case of funds that are distributed by several banks in the sample and were therefore collected more than once, the costs are only included in the average cost calculation on a single-weighted basis.

The gross investment amount serves as the cost basis for the upfront fee. The net investment amount is taken as the cost basis for the ongoing fee. This is calculated from the gross investment amount minus the upfront fee. For the sake of simplicity, it is assumed that the net investment amount is constant over the entire holding period; the performance therefore offsets the costs of the fund. Annex 4 analyses the extent to which the results change if performance is assumed to be based on the historical ten-year performance.

The product-dependent cost of advice K_m^{Advice} consist of the initial costs in the form of the $K_m^{Initial}$ as the upfront fee as well as the ongoing fee $K_m^{Ongoing}$.

Thus, the following applies to the product-dependent cost of advice for the commission-based model

$$K_m^{Advice}(a,t) = a * (K_m^{Initial} + t * K_m^{Ongoing})$$

depending on the investment amount a in € and the investment horizon t in years for the product classes $m \quad M = \{Equity\ fund,\ Mixed\ fund,\ Bond\ fund\}$ with

$$K_m^{Initial} = \sum_{i=1}^{n} A_{m,i} * G_{m,i}$$

and

$$K_m^{Ongoing} = \sum_{i=1}^{n} Z_{m,i}^{Laufend} * G_{m,i}$$

where $A_{m,i}$ is the upfront fee, $Z_{m,i}^{Ongoing}$, the inducements from the ongoing product and service costs and $G_{m,i}$ the weighting factor of the respective fun i of the product class m.

Since investment advice is not usually provided at the level of individual products but rather on the basis of the client's overall portfolio, the product-dependent costs of advice are aggregated at the portfolio level in the next step. The costs of advice for the overall portfolio are calculated by weighting the product-dependent cost of advice by the portfolio share p_m of the respective fund class:

$$K_{Commission}^{Advice}(a,t,p_m) = \sum_{m \in M} K_m^{Advice}(a,t) * p_m$$

[92] By way of comparison, the sample covers 16.15% of total net fund assets as at the reporting date of 31 December 2020. However, a large part of the total assets is characterised by existing business, which is why the net funds inflow is the more suitable indicator for the analysis of sales activity.

[93] The detailed methodology can be found in DDV (2017). The data were collected by DDV for the second half of 2020 and made available to KPMG.

[94] The share is 23% according to the ECB; cut-off date: 31.12.2020.

The costs of advice for the fee-based model result from the average hourly rate S, the duration of the advisory meeting $D_{Initial}$ or $D_{Ongoing}$ or H. Due to the fixed hourly rate, the costs of the fee-based model are independent of the investment amount and the portfolio allocation. It is assumed that the investor receives advice before the portfolio is liquidated at the end of the investment horizon.

This results in consulting costs of

$$K_{Fee}^{Advice}(t) = D_{Initial} * S + D_{Ongoing} * S * t * H$$

In order to enable comparability with the commission-based model, it is assumed that the product and service costs (with the exception of the upfront and ongoing fees) of the fee-based model are identical to those of the commission-based model. The services offered under the advisory models are also assumed to be comparable.

The costs of advice of the two models are then compared by means of a break-even analysis. This determines the point at which the costs of commission-based and fee-based advice are balanced, based on the investment amount. The break-even point can also be visualised graphically as the intersection of the cost curves of the two models.

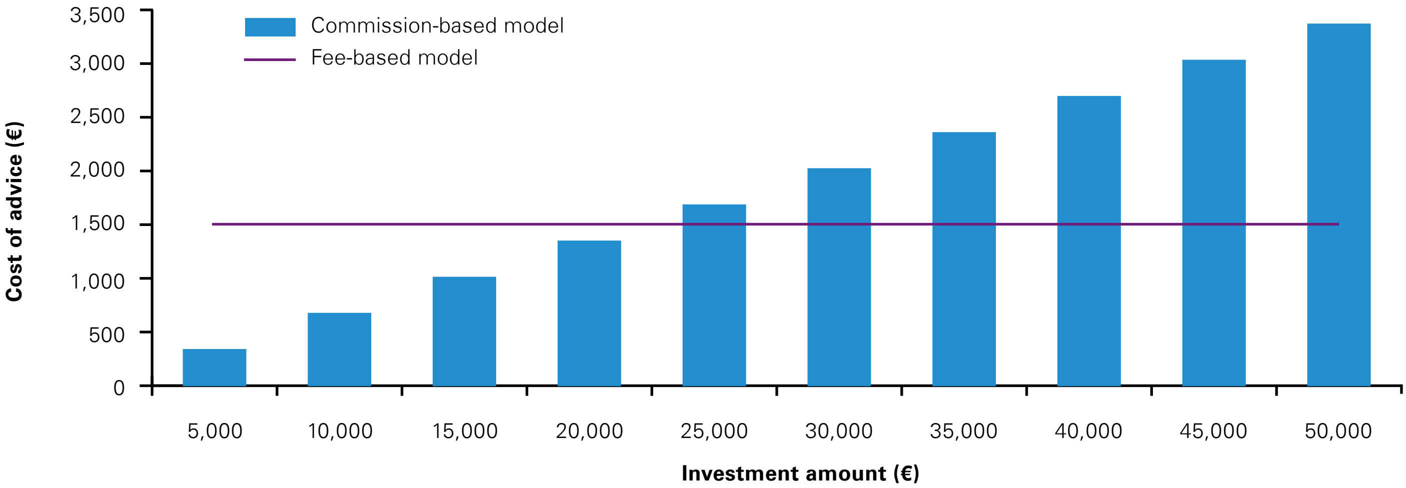
The break-even point results from

$$K_{Commission}^{Advice}(a,t,p_m) = K_{Fee}^{Advice}(t)$$

As part of the cost comparison, one of the variables (investment amount, investment horizon) is kept constant in each case in order to determine the break-even for the remaining variable. The assumptions made for this purpose on the basis of the characteristics of retail customers are explained in Section 2.2.

Annex 4: Comparison of cost of advice taking into account product performance[95]

Cost of advice (€) for an investment horizon of 6.5 years, by investment amount (€), incl. performance



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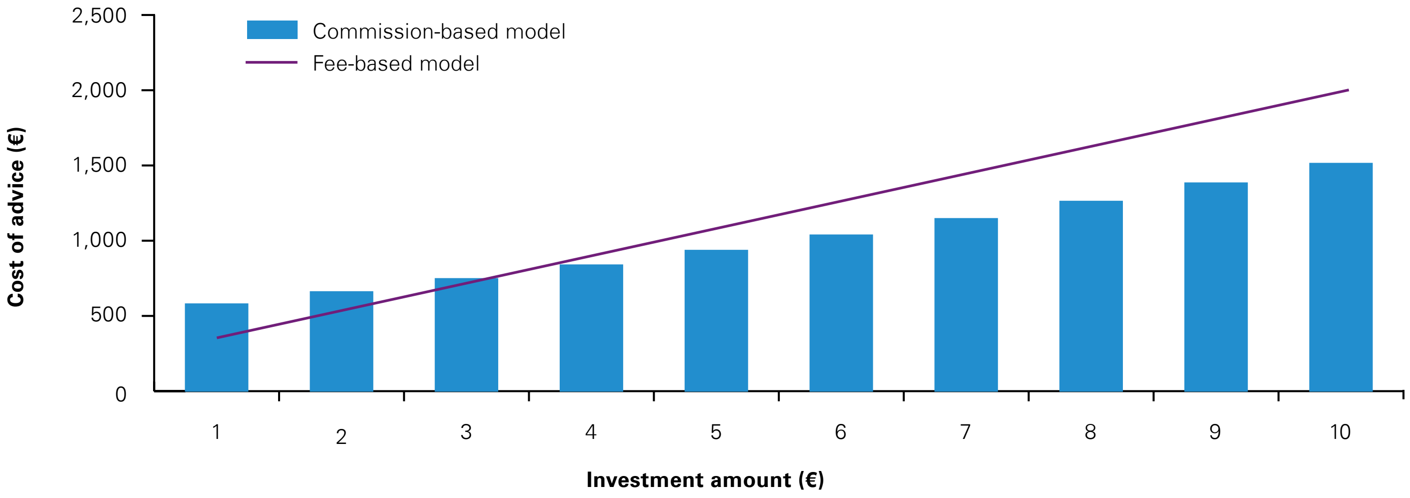
95 Only the performance of the funds was taken into account; due to the varied product range, non-inducement-bearing products and certificates are difficult to evaluate and, with a 15% share of the portfolio, are not significant for the overall performance of the portfolio..

Cost of advice (€) for a median-investor, by investment horizon (years), incl. performance



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Contact

KPMG AG
Wirtschaftsprüfungsgesellschaft

Christoph Betz
Partner, Financial Services
T +49 69 9587-4347
christophbetz@kpmg.com

Thomas Matis
Senior Manager, Financial Services
T +49 89 9282-6377
tmatis@kpmg.com

www.kpmg.de

www.kpmg.de/socialmedia