INTRODUCTION

This is the last Kandlbinder report that will be written by Dr Hans Karl Kandlbinder, who retires after more than 30 years of producing this annual analysis of the Spezialfonds, now used extensively by institutional investors in Germany. In that time, the report has become the source of information about this highly unique vehicle that has served its marketplace well. Understandably, the progress of the industy is now at a lower rate than it has been. Assets at the end of 2001 amassed in Spezialfonds came to €507bn, down somewhat on the previous year.

This year, Dr Kandlbinder (photo left) has a co-author, Till Entzian, a 39-year old lawyer, based in Frankfurt, who is a specialist in advising investment fund companies. His credentials are impeccable, having developed an exceptional understanding of investment regulation when working for the BVI, the German investment funds association, over a seven-year period. He had experience there on the international affairs and securities investment before he became co-responsible for development and interpretation of domestic investment regulation and investment tax rules. He then joined Union Investment Institutional, also in Frankfurt, which provides Spezialfonds services to the German mutual sector. Starting next year, he will continue with the report following the retirement of Dr Kandlbinder.

This year, we again bring to readers of *IPE* our English-language translation of the report which was published this summer in German in *Zeitschrift fur das gesamte Kreditwesen* by Frankfurt-based publishers Fritz Knapp Verlag.

For the purposes of this translation, we have used the term 'specialised investment funds' for Spezialfonds. This is an open-ended investment fund under the German Investment Act (Gesetz uber Kapitalanlagegesellschaften – KAGG). The main difference between a specialised investment fund and an open-ended investment or mutual fund available to the public is in the fact that a specialised investment fund belongs exclusively to the investors, who cannot number more than 10, and who are not individual persons, but have a legal form such as a corporation, foundation, institution or association. In fact, most funds are set up with just one or two institutions as investors. There are in addition normally certain tax and accounting advantages. Through an investment committee, usually formed when establishing the fund, the investor has the opportunity to influence the investment policy of the fund.

Though sponsored by the investor, each fund is set up and run through a Kapitalanlagegesellschaft (KAG), which is an investment management company operating under banking law. The term KAG has been has been translated here as 'investment trust company'.

Published as a supplement with September 2002 issue of Investment and Pensions Europe.

IPE International Publishers Ltd, 320 Great Guildford House, 30 Great Guildford Street, London SE1 0HS
Tel: +44(0)20 7261 0666, Fax: +44(0)20 7928 3332, Web site: www.ipeonline.com, ISSN 1369-3727

Still on moderate growth track

By Hans Karl Kandlbinder and Till Entzian

The capital market statistics published at the end of February by the German Bundesbank finally revealed that for the calendar year 2001, and for the first time in the 34 year history of the specialised investment fund (*Spezialfonds*), this investment instrument had recorded a fall in fund volume. Though the fall was not very great (Table 2), in fact only 1.4%, it was still a fall. But this is not the beginning of the end for specialised investment funds.

At first sight, this first-ever downturn in specialised investment fund volumes may seem surprising, but in no way does it mean that this investment segment is entering a negative phase, as a closer analysis shows that there is absolutely no justifiable reason for the fall. On the contrary: the decline in specialised investment fund volumes is the consequence of the downward trend on global capital markets during 2001, where specialised investment funds still held up relatively well. Although net receipts also fell in 2001, by 9.1% compared to the year before (Table 1), the decline was not as sharp as the 23.6% seen in 2000 as against 1999. In any case, net receipts of €41.3bn in absolute terms is still a very respectable figure, so we can rather talk of a consolidation in the specialised investment funds market at a fairly high level.

The specialised investment fund success story

In the Bundesbank statistics for 1968, the specialised investment fund investment model appeared for the first time as 'individual funds', with 13 funds and a total volume of DM147m, ie, with an average volume for each fund of DM11m and a 2% share of the whole investment funds market. They became an overwhelming success. Just 20 years later, in 1989, there were 1,474 specialised investment funds with a volume of DM108bn and a 50% share of the whole investment funds market, which had been achieved as early as 1986. The boom continued uninterrupted until 1998, when the volume of specialised investment funds stood at over €372bn, representing 64.3% of the total volume of the investment fund market. At that time, 52 investment trust companies (*KAG: Kapitalanlagegesell schaft*) from seven financial groups had set up 4,238 securities-money market-based specialised investment funds, 739 of them that year. This resulted in almost three new specialised investment funds being established for each banking day and the growth in volume from the previous year, 1997, was over 31%. However, the process of switching to the 'newer' investment trust companies of the savings banks (Sparkassen) and central savings banks (Landesbanken) sector, the co-operatives, the insurance industry and foreign bank subsidiaries had begun; it is still happening.

The net receipts for 2001, at €41.3bn, are at a level between the (then) boom years of 1996 and 1997, and therefore really signifies a consolidation rather than a step backwards. In 2001, in the final analysis, 224 new specialised investment funds were set up by 73 investment trust companies (14 with specialised real estate investment funds), which gives an average of just under one new specialised investment fund per banking day – more of a 'recuperation' than an otherwise overheated development.

The negative effect of the capital market collapse

The decisive negative effect of the collapse of the capital markets can be seen most clearly from an examination of Chart 2, based on the Bundesbank statistics, in which the effective global changes in value are determined for the specialised investment funds from earnings distribution and net receipts in relation to the respective fund volumes. Since we have been carrying out these special analyses (since 1997), such effective negative changes in value are quite unprecedented. It was solely in the case of the equity-based funds that had there been any hint of this the year before. For 2001, these changes in value on the respective computed fund volume, in the case of the equity-based funds, amount to a fall of 13.6% and even for the mixed specialised investment funds to a fall of 8.3%. Only the bond funds were ahead at the end of 2001, by 3.2% on the computed fund volume.

The fairly strong net receipts for specialised investment funds in 2001 have, in any case, not only prevented further falls in volume induced by the stock market downturn. They have also shown that investors in specialised investment funds, at the same time, operate anti-cyclically and have therefore shown themselves to be true professionals.

Smooth passage for securities-based specialised investment funds

While securities-based specialised investment funds of all kinds continued to report healthy, albeit moderate, growth in terms of funds numbers and receipts during 2001, and the specialised real estate investment fund instrument saw a boom in 2001 and up to very recently (Kandlbinder/Entzian, *"Der Immobilien-Spezialfonds in Entfaltung"* ["The evolution of the specialised investment fund"] in: *Immobilien & Finanzierung* volume 13/2002), the latest trends in the case of the securities-based spe-

Table 1: New fund inflows to investment trusts (Total new inflows per year = 100)

	German investment funds open to the general public (all fund types, with the exception of real estate funds)		German real estate open to the general public		German specialised investment funds (including specialised real estate investment funds)	
Year	DM m*	% share	DM m*	% share	DM m*	% share
1969	3,376	86.5	-	-	528	13.5
1975	1,486	48.6	163	5.3	1,407	46.1
1989	15,943	47.9	492	1.5	16,839	50.6
1993	6,075	9.8	14,716	23.9	40,881	66.3
1995	9,856	18.2	6,921	12.8	37,294	69.0
1996	2,567	3.3	13,950	17.6	62,592	79.1
1997	25,065	18.1	6,436	4.6	107,445	77.3
1998	34,308	20.2	4,690	2.8	130,750	77.0
in €	17,541			2,398	66,851	
1999	30,289	31.2	7,395	7.6	59,513	61.2
2000	42,536	49.9	-2 824	-3,3	45,448	53.4
2001	25,363	33.0	10,159	13.2	41,289	53.8

Source: Deutsche Bundesbank, Capital Market Statistics, Table page 54 *In euros from 1999

Table 2: Investment trust companies: number of funds and fund assets

	German investment funds open to the general public (all fund types, with the exception of real estate funds)			German real estate open to the general public			German specialised investment funds (including specialised real estate investment funds)		
As at year end	No of funds	DM m*	% share	no of funds	DM m*	% share	No of funds	DM m*	% share
1968	31	6,257	97.7	-	-	-	13	147	2.3
1975	95	15,307	66.8	9	2,751	12	233	4,849	21.2
1989	254	105,989	46.1	12	16,070	7	1,474	107,752	46.9
1993	470	137,737	33.0	15	44,254	10.6	2,207	235,038	56.4
1995	594	194,310	34.4	15	59,856	10.6	2,624	310,780	55.0
1996	637	212,289	31.0	15	74,224	10.9	2,958	397,514	58.1
1997	716	264,154	29.3	16	81,026	9	3,508	555,121	61.7
1998	788	318,192	28.1	17	86,220	7.6	4,245	728,213	64.3
in €		162,689			44,084		372,329		
1999	909	236,589	30.9	18	51,363	6.7	4,829	478,129	62.4
2000	1,099	258,054	31.4	20	48,931	6.0	5,328	514,226	62.6
2001	1,253	247,131	30.4	22	59,249	7.3	5,550	506,912	62.3

Source: Deutsche Bundesbank, Capital Market Statistics, Table page 52 *In euros from 1999

Table 3: Breakdown of assets of securities-investing specialised investment funds

As at end of year	Total	Debt securities*[1] Domestic	Debt securities*[1] Foreign	Shares*[2] Domestic	Shares*[2] Foreign	Money market instruments (and other secs)	Cash reserves debenture loans and other assets less obligations
				DM bn			
1995	306	172	27	59	20	2	27
1996	393	207	37	82	35	3	29
1997	550	249	59	132	68	4	38
1998	722	302	81	140	140	5	54
in Euro	369	154	41	72	72	3	28
1999	473	160	63	80	139	3	28
2000	507	163	85	60	166	3	31
2001	497	157	112	44	143	4	38
				% share			
1995	100	56	9	19	6	1	9
1996	100	53	9	21	9	1	7
1997	100	45	11	24	12	1	7
1998	100	42	11	19	19	1	8
1999	100	33.9	13.4	16.9	29.3	0.6	5.9
2000	100	32.0	16.8	11.8	32.7	0.6	6.1
2001	100	31.5	22.6	8.8	28.8	0.7	7.6

1) Including convertible bonds and the like
2) Including rights issues, mining shares, participation certificates and the like
Differences in the total result from rounding of figures. Source: Deutsche Bundesbank, Capital Market Statistics
* The classification is based on issuers (not on currencies)

cialised investment fund show a much calmer situation. In the first quarter of 2002, the number of securities-based specialised investment funds fell, on balance, by effectively eight funds. This figure is based on the following:

- 11 bond funds,
- four equity-based funds,
+six mixed funds,
+ one fund of funds and receipts by securities-based specialised investment funds over this period totalled only €4,297m. Interestingly, at the beginning of 2002 the specialised money market investment funds doubled in number, from five to 10 funds, and in January 2002 alone exactly €300m of new money flowed into, or rather were parked in the specialised money market investment funds. These receipts represent no less than three-fifths of the total amount that was received by specialised money market investment funds during 2001.

Continuous trend into foreign investments

Profiting from the liberalisation of the statutory investment regulations and from the creation of the Euro-zone, the trend (Table 3) into non-German investments by the specialised investment funds continued inexorably, and by the end of 2001, for the first time, had easily topped the 50% mark, at 51.4%. This trend had been evident since 1996, when the share of foreign investments by the specialised investment funds has developed as follows:

1996	18.0%
1997	23.0%
1998	30.0%
1999	32.7%
2000	49.5%
2001	51.4%

as at end March 2002
52.8% (Chart 1)

In fairness, it must also be said that this trend to non-German investments is not just being actively driven by the investors themselves, but is also being passively assisted, in statistical terms, by the following phenomenon: an investment in Hoechst stocks, for example, was quite clearly an investment in Germany; since Hoechst became Aventis, with its group headquarters in Strasburg, in the Bundesbank's capital market statistics it is now regarded as an investment in Europe, not Germany. Mannesmann/Vodafone or Kamps/Barilla are similar examples. But of course, for German institutional investors, too, the investment market base has expanded, from Germany into Euroland – a trend that will continue, especially if the UK, hopefully in the not too distant future, becomes part of Euroland.

The development of the other, virtually secular trend of investments by specialised investment funds in recent years has not been so clear-cut, namely the trend towards increased investment in equities, and here again mainly in non-German equities. The market setbacks during 2001 may have halted this trend, albeit only temporarily, but in other respects the tendency is quite clear (Table 3, in conjunction with Chart 1).

Non-German investors noticeable only in specialised real estate investment funds

Non-German investors have otherwise continued, for the third year in succession, to move out of their investments in German securities-based specialised investment funds (Chart 3). The situation is different, however, in the case of specialised real estate investment funds: at the end of 2001, non-German investors' holdings still totalled €1,439m, 16.4% of the total volume of €8,778m; in terms of net receipts by specialised real estate investment funds, too, in 2001 non-German investors accounted for €310m, or 13.6% of the total receipts by the specialised real estate investment funds amounting to €2,274m.

On the structure of holders of specialised investment funds

This year, it is satisfying to note that all 59 investment trust companies (ITCs) (all 54 members of the German Federal Association of Investment Companies, plus the five ITCs that issue specialised investment funds but are not members of the Association) took part in the authors' 2001 year-end survey of investment trust companies. As at the end of 2001, according to Bundesbank statistics, these companies were managing some €498,155.1bn of the specialised investment funds volume in 5,501 funds (excluding specialised real estate investment funds) (Table 4). Accordingly, it was possible once again to include 100% of the specialised investment fund volume in the survey. The analysis of the survey results shows a figure of €498,010m being managed in 5,514 funds, which means that there are slight differences from those given in the Bundesbank statistics, but these can certainly be disregarded and is quite easy to explain in view of the magnitude of the figures involved.

Chart 1: Distribution of capital of securities-investing specialised investment funds as at March 2002

	€m	%
Total funds volume	499,280	100
Debt securities		
domestic	153,783	30.8
foreign	115,957	23.2
Shares		
domestic	45,484	9.1
foreign	147,811	29.6
money market instruments	344	0.1
Cash reserve (including debenture loans and other assets less liabilities)	35,901	7.2

Number of funds up by only 4 %

In the first place, it must be noted that in 2001, while the number of funds increased by a modest 4%, the specialised investment funds market (excluding specialised real estate investment funds) shrank in terms of funds volume by almost 2%, from €507,839m to €498,134m, according to the Bundesbank's figures, and from €507,995m to €498,010m according to the results of our survey.

In this market, the relative sizes of the investor groups are as follows:

1. The insurance industry and institutional pension funds still constitute the most important investor groups, with a 52.9% share of specialised investment funds volume (previous year 52.7%); their shares have fallen in absolute terms by €4.04bn in specialised investment fund placements, compared to + €70.1bn the previous year, but are still inching back to the peak 53.2% share achieved in 1997. The insurance companies investor group in particular, with €7.2bn less in terms of specialised investment fund volume in 2001, is more affected than the institutional pension funds investor group, whose share of specialised investment fund volume rose between 2000 and 2001 both in absolute terms (+ €3.13bn) and in relative terms, from 14.2 to 15.1%.
2. While the second most important investor group of business enterprises, which can be subdivided into two distinct subgroups, again failed to maintain the relative shares of the previous year in overall terms, a detailed view of the situation shows a completely different trend:

❑ what are known as the banks' own security deposit funds, with a share of the specialised investment funds volume rising to 24.6% (or in absolute terms + €748m new spe-

Chart 2: Specialised investment funds (excluding specialised money market and real estate investment funds): distribution of income, net sales receipts and effective change in value (all figures in €m)

	Bond funds	Equity funds	Mixed funds	Fund of funds	All
Funds volume at 12/00	132,334	59,330	315,568	514	507,746
Less income distributed in 2001	-5,663	-1,765	-10,312	-7	-17,474
Sub total	126,671	57,565	305,256	507	489,999
+ net sales receipts in 2001	+13,634	+2,604	+22,134	143	+38,515
Computed funds volume at 12/01	140,305	60,169	327,390	650	528,514
Actual values of funds volume 12/01	144,825	51,989	300,117	609	497,540
Effective change in value*					
of funds volume in 2001 versus	+4,520	-8,180	-27,273	-41	-30,974
position as at 12/00	(+4,582)	(-1,230)	(+7,290)	(-)	(+10,244)

(Corresponding figures for previous year in brackets)
Source: Deutsche Bundesbank, Capital Market Statistics p52 + 53. Minor differences in total as a result of rounding.
Because the last column "All" also includes holding funds and mixed securities and property special assets, which are not recorded separately, the addition across the individual lines may not agree with "All"; thus, in the line "Actual value of funds volume 12/00" the 'All' total is greater by precisely €514m than the cross total of the previous columns because this represents the volume of the 20 specialised holding funds as at 12/00.
*Note: it must be stressed that this calculation cannot be used to ascertain what has already been realised in the funds

cialised investment fund placements, compared to + €16.4bn the previous year), in which the savings banks and co-operatives sector institutions are particularly strongly represented;

❑ those business enterprises whose share of the specialised investment funds volume has fallen to 12.7% (compared to 14.3% the previous year), and whose specialised investment fund placements serve largely as 'capital with societal restrictions on individual property rights', that is, the 'funding' for pension provisions (in absolute terms, receipts of these specialised investment fund placementswere fell by €9.3bn, having already fallen by €4.7bn the previous year).

3. The relative share of the group of other licensed specialised investment funds investors has again risen, to 8.1%, compared to 7.1% the year before, and in absolute terms the total sum invested has increased by €4.13bn (previous year, plus almost €6bn).

4. Placements in specialised investment funds by the social insurance institutions group have fallen in absolute terms by €424m, compared to the previous year, but has maintained the 1.3% relative share of the previous year. Placements in specialised investment funds by the social insurance institutions group have therefore fallen back to the low levels of 1997 and 1998.

Once again, fewer non-German holders of specialised investment funds

5. The specialised investment fund volume allocable to the foreign group of specialised investment fund holders has fallen by one-third, to a relative share of 0.4% (previous year 0.6%). Analysis of another set of statistics from the Bundesbank (Chart 3) even shows that during 2001 there were in effect substantial flowbacks from specialised investment funds by non-German investors, even though the number of specialised investment funds held by non-German investors has fallen, albeit only slightly. The reluctance of non-German investors to participate in the specialised investment funds sector (excluding specialised real estate investment funds) remains a phenomenon, which is difficult to explain rationally, especially if we consider how heavily non-German institutional investors are committed to direct investment on the German capital market.

Explainable differences from the Bundesbank statistics

If we consider the fact that the aggregation categories between the Bundesbank and the authors' survey are different and dissimilar in coverage, it may be confidently stated that the results are *de facto* not that different, as may be discerned from Table 5 in the 'Crossovers from the author's survey to the Bundesbank statistics'. In relation to the scale, demarcation differences of several billion euros can effectively be disregarded. The Bundesbank's heading 'insurance companies', excluding the heading 'occupational pension schemes', shows around €18.4bn less than the authors' insurance companies plus institutional pension funds investor groups, which incorporate the occupational pension schemes. By contrast, under the Bundesbank's heading 'social insurance institutions' there are around €6.2bn more than in the 'social insurance institutions' group as defined by the authors, which excludes public supplementary pension funds, because in our survey the public supplementary pension funds are included in the 'institutional pension funds' group. As in the previous year, the heading 'other enterprises' remains the largest difference in relative terms, with the Bundesbank statistics showing some €22.5bn more than the results of the survey by the authors, although for the 'credit institutions', with approximately €4.9bn more in the Bundesbank statistics, the difference is hardly crucial, any more than are the €172m less shown in the Bundesbank statistics for non-German specialised investment fund holders than in our study.

Different system-based approaches

Apart from the various types of classifications in the Bundesbank statistics on the one hand and the authors' survey on the other, other system-based approaches may also produce different results. For example, the corresponding Bundesbank questionnaire only leaves room on the pre-printed form 10380 for one kind of unit-holder under the heading 'unit-holder type', which – if there are more than one – the main type of unit-holder then has to check. In their survey, however, we intentionally emphasise in each case the exact volume of the funds sources per fund for each individual unit-holder.

This different system, therefore, certainly makes it possible, to give an extreme example, for three specialised investment funds with volumes of three times one hundred units. These predominantly belong to one investor from the insurance branch, but 49% of whose volume is, in each case, held by non-German investors, are shown, quite correctly, in the Bundesbank statistics at 300 volume units under the investor heading 'insurers'.

In our survey, these are shown as 153 units for the insurance investor group, on the one hand, and as 147 units for the investor group 'foreign specialised investment fund holders'. So in practice, it certainly seems from the Bundesbank's data that, over the course of time, in the case of specialised investment funds which have an ownership of 51 to 49, the 'predominant indicator' has to be changed the next month, even where the inflow of resources from one holder is insignificant.

Market shares of specialised investment fund providers

Once again, the insights shown by the distribution of the ITC groups' market share as at the end of 2001

Table 4: Structure of specialised investment fund holders as % of funds volume (all fund types, with the exception of specialised real estate funds)

		End 2001 %	End 2000 %	End 1999 %
I-V	Domestic holders of specialised investment funds			
I	Insurance enterprises – total insurance industry ie, private insurance enterprises (and those incorporated under public law)	37.8	38.5	35.1
II	Social insurance institutions – statutory state social insurance institutions	1.3	1.3	2.1
III	Total institutionalised old-age pension schemes, ie, pension funds, benevolent funds, occupational, official and/or employee pension schemes	15.1	14.2	17.1
IV	Business enterprises, ie, financial investments for capital with societal restrictions, on individual property rights de facto for "funding" of pension provisions and general financial investments	37.3	38.3	38.6
	(Of which credit institutions' "own security deposit funds")	(24.6)	(24.0)	(22.3)
V	Other licensed specialised investment fund holders, ie, churches, foundations, religious-charitable bodies, associations, trades unions	8.1	7.1	6.4
VI	Foreign specialised investment fund holders	0.4	0.6	0.7
		100.0	100.0	100.0

Result of a survey by the authors
Note: For 2001, 59 (out of 59) ITCs which have issued specialised investment funds were again recorded, which is 100% of the whole volume (in all of the previous years, 100% or 99.979% of funds volume)

are informative (Tables 6, 7 and 8). With the volume of the specialised investment funds market as a whole, excluding specialised real estate investment funds, having contracted by 1.97% (compared to increased volumes of 7 and 28% in the two previous years) the previous trends of the relative shifts in market share are continuing, but rather less emphatically than before, in some cases, and in other cases they too are shifting.

The specialised investment funds volumes of the investment trust companies of the major/regional banks are shrinking particularly sharply. The decrease covers both the fund numbers and the fund volume, as well as the relative market share, which has fallen to well below 30% – the first time this has happened with this provider group. The investment trust companies of the private banks, by contrast, have managed a straight reversal of the trend with a threefold increase in fund numbers, fund volume and relative market share.

The investment trust companies of the savings banks and central savings banks are growing, counter to the general trend of shrinking volumes, and have for the first time increased their market share to well over one-fifth. The ITCs of the co-operative banks, at a relatively low level, have also done much better than the volume trend, improving their position in the market to 6%, which means that for the fourth consecutive year they have gained market share, having started in 1996 with a share of under 5%.

Once again, in 2001, the biggest jump in specialised investment funds has been by the 16 investment trust companies that represent insurance interests: number of funds up 8.9%, fund volume up 2.8% and market share now up to 20.4%. The insurance ITCs have therefore now become the second-largest providers in the market, just managing to oust the ITCs of the savings banks and central savings banks from this position in 2001.

Further restructuring in insurance company ITCs

The fact that insurance companies shifted huge volumes from specialised investment funds during 2001 into their own investment trust companies can also be deduced from the investment statistics of the federal supervisory office for insurance companies (BAV): figures published quarterly in the BAV's official bulletins, for instance, show not only substantial new placements by the insurance companies in specialised investment funds, but also a considerable number of fund closures (Chart 4).

This chart means, quite simply, that in 2001 a good 58% (compared to over 40% the previous year) of gross investments in specialised investment funds by the insurance companies are derived from fund closures.

The number of insurance ITCs remained the same in 2001 as in the previous year (at 16), although there was one name change, from Talanx to Ampega.

In 2001, the growth of specialised investment funds among those investment trust companies that are subsidiaries of foreign banks was much less spectacular than it had been the previous year. One investment trust company has left this group, as it now no longer sets up specialised investment funds, only funds open to the general public (CDC, now renamed Swiss Re Asset Management). The remaining 16 investment trust companies in this group were generally unable to continue the upward trend of previous years: although the number of managed specialised investment funds increased by a further 5.5% in 2001, in terms of funds volume this group fell by 3.8%, as a result of which its relative market share has fallen slightly from 7.1% to 7.0% now.

In 2001, the heterogeneous group of 'other investment trust companies' fell in both absolute and in relative terms (market share now just 3.5%, compared to 4.2% and 4.7% in the two previous years). However, is still significant because of the heavyweights it includes (Siemens KAG and Postbank Invest), and it has been much talked about over the past year as a result of an interesting new development.

The second half of 2001 saw the establishment of Lupus alpha Kapitalanlagegesellschaft mbH in Frankfurt. The company has been set up on a partnership basis, is owned by private investors and cannot therefore be classified with any of the existing ITC groups (belonging to banks/credit institutions, insurers, foreign providers). By the end of 2001, Lupus alpha had already set up two specialised investment funds, in addition to four funds open to the general public, and its advertising is based on the reasoning that it is independent of credit institutions, insurers, industrial enterprises and foreign providers, and that five partners, who together own 50% of the capital, therefore also act as the senior managers of this investment trust company. It will be interesting to follow the development of new asset management concepts of this type on the market. In any event, with its three funds open to the general public and two specialised investment funds, the Düsseldorf-based GWA Gesellschaft für Wertpapieranlagen-GWA-mbH, which has been around for a long time, and is not unsimilarly structured, has remained relatively stable for years.

Chart 3: Securities-investing specialised investment funds held by non-German investors

	in 1999 as at 12/99	in 2000 as at 12/00	in 2001 as at 12/01	in 2002 as at 03/02
Number of funds	47	47	45	44
of which:				
bond funds	15	14	15	14
equity funds	8	10	8	8
mixed funds	24	23	22	22
Sales receipts €m	-146	-720	-318	9
of which:				
bond funds	+174	-35	-167	-6
equity funds	-257	+6	-114	-3
mixed funds	-63	-692	-37	18
Fund volme €m	3,299	2,586	2,201	2,201
of which:				
bond funds	918	913	925	917
equity funds	406	388	189	188
mixed funds	1,974	1,285	1,087	1,096

Source: Deutsche Bundesbank, Capital Market Statistics, statistical supplement to monthly report 2, Table VI investment trust companies /5, number, sales receipts and capital of domestic specialised investment funds by unit holders and application of earnings. Differences in the totals result from rounding of figures

Microanalysis of market shares by ITC groups

The view of the global market share is even more informative if the market segments are arranged with the individual ITC groups and then broken down accordingly, as in Table 9. However, it has been taken into consideration that in the ITC groups of the co-operative banks, firstly, and secondly of the 'others', there are only a few ITCs in each, of which again in each case one or two dominate in terms of volume in such a way that individual conclusions may be drawn. With the classification of market share on the basis of structure of the specialised investment funds holders (Table 4) to the ITC groups as defined in Table 6, both of the ITC groups referred to above (co-operative banks and 'others') have therefore been omitted.

Even if 'only' 90.6% of the whole specialised investment fund volume is included in the survey, Table 9 nevertheless provides some surprising insights, because for each ITC group observed, the whole fund volume of the ITC group concerned is recorded and hence the comparison with a range of previous years is now possible.

Some marked, but interesting shifts

The shifts in the investor structures for each of the ITC groups in 2001 were at times quite marked compared to 2000, and the following points stand out:

1. The insurance industry is still, naturally, most strongly represented 'among its own kind' with

Table 5: Crossovers from the authors' survey (table 4) to the Bundesbank statistics

	2001 €m	2001 in %	2000 €m	2000 in %	1999 €m	1999 in %
Domestic specialised investment fund holders	495,934	99.56	504,646	99.49	470,213	99.31
Insurance enterprises (including pension funds and occupational retirement schemes)	244,987	49.18	255,531	50.38	239,222	50.52
Social insurance institutions and official supplementary pension funds	12,508	2.51	12,050	2.38	13,426	2.83
Other companies and banks	213,439	42.85	212,814	41.95	195,407	41.27
(of which banks)	127,586	25.61	124,874	24.62	110,994	23.44
Non-profit making private organisations and others	24,999	5.02	24,250	4.78	22,207	4.69
Foreign specialised investment fund holders	2,201	0.44	2,586	0.51	3,299	0.69
Total	**498,134**	**100**	**507,232**	**100**	**473,511**	**100**

Table 6: Specialised investment funds (excluding specialised real estate investment funds) by ITC groups as at year end 2000 and 2001

Year end 2001

Investment trust companies of	Number: Investment trust companies	Number: Funds	Funds volume: €m	Funds volume: %
Major and regional banks Aii (=Allfonds-BKG), BB, Commerzinv., dbi, DeAM, DVG, Nordinvest	7	1,758	142,590	28.6
Private banks Frankeninvest, FTI, Inka, MI, Monega, OKAG, Universal, Warburg	8	793	71,084	14.3
Savings banks and central banks Bayern, DIM, HelabaInvest, SüdKA, West AM	5	1,485	100,812	20.2
Co-operative banks DEVIF, Union	2	501	29,879	6.0
Insurance interests Allianz, AL, AM Generali, Ampega (=Talanx), AXA, BWK, Delta Lloyd, GCR, Gerling, Hansinvest, MAM, MEAG, MK, Nordcon, Swisslife, Zurich	16	429	101,797	20.4
Foreign bank subsidiaries ABN Amro, BNP Paribas, Citigroup AM, CSAM, DG Panagora, Goldman Sachs, INVESCO, JP Morgan, Julius Baer, Lazard, Merck Finck, MLIM, SEB Invest, SSG, UBS, Veritas SG	16	497	34,696	7.0
Others GWA, MAT, Postbank, Siemens KAG, + Lupus Alpha	5	51	17,152	3.5
Total*	**59**	**5,514**	**498,010**	**100**

Year end 2000

Investment trust companies of	Number: Investment trust companies	Number: Funds	Funds volume: €m	Funds volume: %
Major and regional banks Allfonds-BKG, BB, Commerzinv., dbi, DeAM, DVG, Nordinvest	7	1,765	154,957	30.5
Private banks Frankeninvest, FTI, Inka, MI, +Monega, OKAG, Universal, Warburg	8	725	69,165	13.6
Savings banks and central banks Bayern, DIM, HelabaInvest, SüdKA, West AM	5	1,407	99,386	19.6
Co-operative banks DEVIF, Union	2	484	28,019	5.5
Insurance interests Allianz, AL, +AM Generali, AXA, BWK, +DLD-SIM, +GCR, Gerling, Hansinvest, MAM, MEAG, MK, +Nordcon, +Swisslife +Talanx, +Zurich	16	394	99,030	19.5
Foreign bank subsidiaries ABN Amro, +BfG- SEB, CDC, DG Panagora, CSAM, Goldman-Sachs, INVESCO, JP Morgan, Julius Baer, Lazard, Merck Finck, MLM, Paribas, Sal. Brothers, SSG, UBS, Veritas	17	471	36,057	7.1
Others GWA, MAT, Postbank, Siemens KAG	4	44	21,381	4.2
Total*	**59**	**5,290**	**507,995**	**100**

Figures from Bundesbank statistics: Federal Association of German Investment Companies and in part surveys by the author – differences in the totals result from rounding of figures.
* While in the case of funds volume and fund numbers there are minor, but explicable differences with the Bundesbank statistics
+ New in specialised investment funds business

its specialised investment funds, and is continuing to build up this share, with a rise of just €1.26bn in 2001 (which is why the share has fallen slightly in relative terms), and then among the ITCs of the private banks, where there have also been signs of a decline (in absolute terms by €281m, in relative terms to 39.2%). The decline in specialised investment fund placements by the insurance industry has been greater among the ITC groups of the foreign bank subsidiaries (down €1.6bn) and among the ITCs of the major and regional banks (down €6.1bn), while the specialised investment placements by the insurance industry among the ITCs of the savings banks and central savings banks have stayed the same in absolute terms (up €9m) and have fallen somewhat only in relative terms.

2. Placements in specialised investment funds by the (German) social insurance institutions (SII) have individually developed in a most idiosyncratic way over the past year, with the general trend downwards (down €425m): the sharp falls in specialised investment fund placements by SIIs have affected mainly the ITCs of the savings banks and central savings banks (down €556m) and those of the major and regional banks (down €194m), while among this investor group some growth has been recorded by the ITCs of the private banks (up €243m), insurance companies (up €214m) and the foreigners (up €76m).

3. Interestingly, in 2001, with higher overall volume (up €3.13bn) institutional pension funds have made advances only with their placements in specialised investment funds among the ITCs of foreign bank subsidiaries (up €678m) and those of the savings banks and central savings banks (up €605m), while all other ITC groups have experienced falls here: ITCs of the major and regional banks (down €5.8bn), private banks (down €142m) and insurers (down €320m).

We can be fully justified in concluding from the strong and still rising proportion of specialised investment funds of this investor group in the foreign bank subsidiary ITCs that those institutionals which are increasingly looking to invest outside Germany and outside the EU/EEA therefore have a particularly strong presence there, because they want to 'buy into' the know-how of the foreign markets from the foreign parent companies of those ITCs.

4. Once again in 2001, however, the most striking fact was a distinct structural change in the business enterprise specialised investment fund holders, and within this group under the heading of 'credit institutions, own security deposits'. While total placements by this group (Table 4) have fallen (in absolute terms by €8.5bn), the trend lines are running in different directions, with the business enterprises on the one side and the credit institutions on the other – and this is even more true if we consider the specialised investment fund placements of these holder groups among the various provider groups in detail.

Placements in specialised investment funds by business enterprises (excluding credit institutions) have grown among the ITC group of the major and regional banks (up by €3.2bn), the private banks (up by €1.6bn) and the insurance interests (up by €735m), but they have fallen among the investment trust companies of the savings banks and central savings banks (down €2.7bn). In net terms, these shifts in the specialised investment fund placements of the business enterprises (excluding banks) resulted in a decrease of €9.2bn in 2001 compared to 2000, which means that there must have been some major changes among the ITC groups not listed in detail here for the reasons explained.

Remarkable developments in own security deposits business of banks

The market for specialised investment funds in the banks' 'own security deposits' business, however, looks quite different. Here, 2001 overall growth was around €750m in 2001, although the distribution is extremely varied: the ITCs of the major and regional banks were down by almost €2.8bn, as were the ITCs of the foreign banks, by a good €400m. By contrast, the ITCs of the savings banks and central savings banks and the private banks were up, by €600m and €250m respectively among the insurance company investment trust companies; here too there is a substantial balance remaining, which is explained by the two ITC groups not reported in detail here.

The ITCs of the savings banks and central savings banks have therefore definitely lived up to their image as the 'own security deposit' service provider for the savings banks (something they actually shied away from in the past), whereas the private bank ITCs and the foreign bank subsidiary ITCs have certainly been very happy with their further success on moving into the own security deposit business.

5. In the case of specialised investment fund management for the investor group of ‘other licensed specialised investment fund holders’, the only winners in 2001 were actually among the ITCs – with the exception of the private banks’ investment trust companies. In this case, the doubling of this investor group’s share of the specialised investment fund pie among the ITCs of the savings banks and central savings banks was particularly noteworthy (from €3,642m at the end of 2000 to €7,597m at the end of 2001).

6. In 2001, the business segment of foreign specialised investment fund holders shrank among all specialised investment fund providers, not only in relative, but also in absolute terms, as has already been noted in the observations on Table 4. The volume of specialised investment funds belonging to non-German investors decreased in 2001 to €2.03bn, from a total of €3.14bn at the end of the previous year.

Average size per specialised investment fund falls again

In this respect, however, the following observation is interesting: the average size per specialised investment fund (excluding specialised real estate investment funds), which had been rising continuously for years, reached its peak level of €99m at the end of 1999, fell for the first time in 2000 (to €96m), and had fallen again at the end of 2001, to €90m. This was general for the branch as a whole (with the exception of the ITCs of the co-operative banks): according to survey, fund assets €498,010m among 5,514 specialised investment funds; the analogous figures for the different ITC groups are shown in Chart 5. This means that the specialised investment fund volumes of the private banks’ ITCs correspond exactly to the branch average, and those of the major and regional banks are just below the average. The specialised investment fund volumes of the insurance interests, at more than two and a half times, are well above the average, while those of the specialised investment

Table 7: Details of shifts in market share 2001 versus 2000 (based on table 6)

	Number of funds: Absolute in units	Number of funds: % change versus previous year	Number of funds: Absolute in units	Number of funds: % change versus previous year
Overall market development of specialised investment funds (excluding specialised real estate investment funds)	+224	+4.2	-9,985	-2.0
Investment trust companies of major and regional banks	-7	-0.4	-12,367	-8.0
Private banks	+68	+9.4	+1,919	+2.8
Savings banks and state banks	+78	+5.5	+1,426	+1.4
Co-operative banks	+17	+3.5	+1,860	+6.6
Insurance undertakings	+35	+8.9	+2,767	+2.8
Foreign bank subsidiaries	+26	+5.5	-1,361	-3.8
Others	+7	+15.9	-4,229	-19.8

Table 8: Development of market share in specialised investment funds (excluding specialised real estate investment funds) by ITC groups 1977-2001

ITCs of	% share of funds volume: 2001	2000	1999	1992	1989	1997
I Major and regional banks	28.6	30.5	34.2	46.1	56	76
II Private banks	14.3	13.6	14.6	18.8	23	12
III Savings banks/state banks	20.2	19.6	19.6	15.0	7	5
IV Co-operative banks	6.0	5.5	5.4	4.0	4	2
V Insurance undertakings	20.4	19.5	15.5	10.8	7	3
VI Foreign bank subsidiaries	7.0	7.1	6.0	5.1	3	-
VII Others	3.5	4.2	4.7	0.2	-	2
	100	**100**	**100**	**100**	**100**	**100**

(basis table 6)

Table 9: Structure of specialised investment fund investors per ITC group as a percentage of funds volume *

Excluding specialised real estate funds and excluding specialised investment funds of co-operative banks and others as at end 2000/2001

Investment trust companies of: respectively as % per ITC group respectively 2000 versus 2001	Major and regional banks 2000 %	2001 %	Private banks 2000 %	2001 %	Savings banks State banks 2000 %	2001 %	Insurance undertakings 2000 %	2001 %	Foreign banks 2000 %	2001 %
I-V Domestic specialised investment fund holders										
I Insurance enterprises – total insurance industry ie, private insurance enterprises (and those incorporated under public law)	26.2	24.2	40.7	39.2	19.6	19.3	89.6	88.4	30.1	26.9
II Social insurance institutions Statutory – state social insurance institutions	2.3	2.3	1.1	1.4	1.3	0.8	-	0.2	1.9	2.2
III Total institutional old-age pension schemes, ie, pension funds, benevolent funds, occupational, official and/or employee pension schemes	21.3	19.1	26.1	25.2	6.6	7.2	4.3	3.9	21.5	24.2
IV Business enterprises, ie, financial investments for capital with societal restrictions, de facto for “funding” of pension provisions and general financial investments	36.9	40.4	23.1	25.6	68.1	65.0	4.8	5.7	38.5	37.8
(of which credit institutions’ ‘own security deposit funds’)	(16.2)	(15.7)	(7.8)	(8.5)	(58.5)	(58.2)	(1.5)	(1.7)	(25.0)	(24.6)
V Other licensed specialised investment fund investors, ie, churches, foundations, religious-charitable bodies, associations, trades unions	12.5	13.5	9.0	8.6	3.7	7.5	0.7	1.4	6.5	7.6
IV Foreign specialised investment fund investors	0.8	0.5	-	-	0.7	0.2	0.6	0.4	1.5	1.3
	100		100		100		100		100	

Results of a survey by the authors

* Table 9 is based on Table 4, classified by ITC groups, as defined in Table 6 – but excluding the ITC groups ‘Co-operative banks’ and ‘Others’, as each of these comprises only two or so ITCs and on the other hand in each case one or two ITCs in the funds volume are more than ‘predominant’.

Chart 4: Movements in insurance companies' capital investment units (=de facto in specialised investment funds) (DM m)

	Gross additions	Disposals	Net additions
Q1 2000	23,385	8,125	15,260
Q2 2000	15,004	7,526	7,478
Q3 2000	12,478	3,960	8,518
Q4 2000	47,856	20,104	27,856
Total 2000	**98,827**	**39,715**	**59,112**
Source: VerBAV 7/00, 10/00, 2/02 und 4/01			
Q1 2001	12,391	5,672	6,719
Q2 2001	7,298	4,061	3,237
Q3 2001	8,126	5,032	3,094
Q4 2001	31,312	19,633	11,679
Total 2001	**59,127**	**34,398**	**24,729**

Source: BAV publications 11/01, 1/02 and 4/02

Chart 5: Average fund assets of investment trust companies (based on table 6)

	Average fund volume		
Investment trust companies of the	as at 12/01	as at 12/00	as at 12/99
Major and regional banks	81	88	95
Private banks	90	95	103
Savings banks and state banks	68	71	73
Co-operative banks	60	58	59
Insurance interests	237	251	226
Foreign bank subsidiaries	70	774	82
Other	336	486	516
Overall average	**90**	**96**	**99**

funds of the foreign banks' ITCs, and those of the savings banks/central savings banks have again fallen well below the average. Only among the co-operative banks' ITCs has the average size of specialised investment increased slightly. The volumes of the specialised investment funds of the 'others' ITC group, by their excessive size, constitute a peculiarity that must be seen for what it is, and even here the average size of their specialised investment funds has fallen perceptibly.

Analysis for insurance companies/pension funds/death benefits funds

If the analysis is done from the 'other side', of the investors – because and to the extent that this is possible through the official bulletins of the former federal supervisory office for insurance companies (VerBAV) and the annual reports of the BAV– the specialised investment fund placements of the largest investor group, namely all of the insurance companies and the pension funds/death benefits funds, Tables 10 to 12 provide some interesting findings. This insurance companies/pension funds/death benefits funds investor group holds more than half of the specialised investment fund volume, which concurs with Table 4 in accordance with the survey we carried out and also *de facto* with Table 5, which is based on Bundesbank figures, and thus in general terms represents the most significant investor group among the specialised investment funds.

Since 1975, when the major amendment to the law on the supervision of insurance undertakings (VAG) took the first steps towards liberalisation and deregulation, combined with more transparent accounting for external observers, even in the case of capital investments, the position of securities separate trust assets underwent some major changes (Table 10). In the interim (from 1990 to 1994), the specialised investment funds, even under their own sub-heading as 'securities-based specialised investment funds' were exactly accessible; since then this has only been possible subsequently, as it were, for direct insurers, and then only in the 'Part B' edition of the BAV annual report. All the same, these publications show that among direct insurers, in the years after 1995, up to as much as 95% of the 'investment units' were comprised of specialised investment funds. That means that the authors' assumption, published for years, that 90% of the 'investment units' item represent all the insurance companies' specialised investment funds is somewhat "understated" for the specialised investment funds.

Advantages of specialised investment funds from the point of view of supervision

In the BAV annual report for 1999 (Part A), the federal supervisory office for insurance companies had already for the first time specifically laid down the special advantages for insurance companies/pension funds/death benefits funds of investing via specialised investment funds: "One advantage of investing in investment units as opposed to direct investment are the more liberal possibilities of investing in investment funds. Additionally, payouts are reported under current earnings, even if they are derived from the realisation of undisclosed reserves within the separate trust assets. Payouts are entered under the so-called 'payment of interest by the association formula."

Three sectors are referred to under 'more liberal investment possibilities':

❏ investment in unlisted securities totalling up to 10% of the separate trust assets

❏ the previously 'legal' raising of restrictive investment limits by full utilisation of the 'underweight' potential investments in separate trust assets that comply exactly with the 'overweight' rule in § 54a paragraph 2 no. 6 clause 1 VAG. However, this advantage will be restricted in future, if not entirely eliminated, by the application of the principle of 'Durchrechnung', calculating through the trust in considering what the trust possesses in securities; and

❏ undertaking financial derivative transactions within the investment funds under the framework of the KAGG investment law.

In these cases, therefore, the insurance supervisory authorities quite correctly put their trust in the provisions of the KAGG and its supervision by the banking supervisory authorities, so that investing in specialised investment funds really does give the supervised company "more liberal investment possibilities" than direct investment.

'Investment directive' causes specialised investment fund providers to rethink (Anlageverordnung)

Since the new directive on the investment of restricted assets of insurance undertakings, or 'investment directive' (AnlV), came into effect on 1 January 2002, the branch of specialised investment fund providers has had to rethink broad areas. But as yet not all of the consequences for contract terms and the management of specialised investment funds for investments derived from the restricted assets of insurance companies and pension funds have been fully discussed, or have yet to be definitively clarified in subsequent regulatory circulars. In any event, the investment directive deals with investments in investment funds (and therefore also in specialised investment funds) more explicitly and in greater detail than did the earlier provisions of the law on the supervision of insurance undertakings (*Versicherungsaufsichtsgesetz*), in section 54a. The equity ratio (and the specialised investment funds will naturally benefit from this as well) is to be raised from the previous 30% to 35%. The former 5% opening clause will also be maintained, and even has an approval option for the regulator of a further 5%, but the 'predominance rules' that we have become so fond of, and regulations covering the so-called 'pure bond-based funds' have been dropped. They have been replaced by more transparent rules that are better able to handle a more realistic evaluation of risk because of the fact that they are calculated through the trust. At least the ratio of the volume of ex-EEA investments has been raised from 6% to 10%, partially to compensate for the former 'predominance rules'. These rules provided the possibility of calculating through the trust in considering what the trust possesses in securities could could relieve the equity ratio in the insurance companies and pension funds, creating room for additional equity-based specialised investment funds, or at least for additional equity volumes in existing specialised investment funds. Initially, however, investment trust companies are likely to have some administrative work: the contract terms for specialised investment funds have to be adapted, both because of the effects of the financial market promotion acts on the KAGG, and also because of the effects of the investment directive on specialised investment funds for investments derived from the restricted assets of the insurance companies/pension funds/death benefits funds. Naturally, the internal reporting to insurance companies/pension funds/death benefits funds which are holders of specialised investment funds will have to be fundamentally reorganised according to the investment.

Insurance companies/pension funds/death benefits funds

In 2001, the significance of the specialised investment funds for the insurance companies/pension funds/death benefits funds investment group increased once again, and can therefore hardly be overestimated:

❏ Out of the total investments by insurance companies/pension funds/burial fund death benefits funds, almost 23% (22.92%, to be exact) A good 15 were invested through investment funds as of December 2001 (previous year 22.34%) and most of these, 20.63% of total investments as at the end of 2001, in securities-based specialised investment funds (previous year 20.11%).

❏ If the heading of securities (that is equities, fixed-interest and fund certificates), which is in any case only 'fund capable' is taken as a reference basis as at the same date in December 2001 (figures in brackets are as at December 2000), the corresponding reference figures as at December 2001 are: 65.55% (62.97%) of securities-based invest-

Table 10: Development of selected capital investment items of insurance companies

Line No.		1975	1991		1995		2000		2001+	
1	Total capital investments in DM bn	162	782		1,117		1,704		943,845	
2	Total capital investments index-linked	100	483		689		1,053		1,140	
3	Total securities items in DM bn	38	220		342		605		330	
4	Total securities items index-linked	100	579		900		1,591		1,699	
5	Total securities items as percentage of line 1	23.5	28.1		30.6		35.48		34.0	
6	Investment certificates items (securities-based investment funds) in DM m	2,275	73,495	64,093*	130,517	117,465**	380,680	342,612**	216,335	194,702**
7	Total investment certs index-linked	100	3,231	2,817	5,737	5,163	16,733	15,060	18,598	16,739
8	Total investment certs as percentage of line 3	5.99	33.41	29.13	38.16	34.35	62.97	56.68	65.55	59.00
9	Total investment certs as percentage of line 1	1.4	9.4	8.2	11.68	10.52	22.34	20.11	22.92	20.63

Source: Annual Reports of the Federal Supervisory Office for Insurance Enterprises (BAV) 1975 to 2000 as well as VerBAV 04/02. *Between 1990 and 1994 it was possible only to extract specialised investment fund certificates from the BAV annual reports: consequently over this period both figures have been given in order to avoid an inexplicable break in the statistics. For the same reason this double entry was continued afterwards (general investment funds/Spezialfonds). It should otherwise be noted that the number of reporting insurance enterprises is not constant over the period. **After 1995 it is again no longer possible to divide the 'investment units', so that specialised investment funds with 90% of the total figure are used, as this mark was close to the specialised investment funds share in 1993 and 1994. The share of specialised investment funds with direct insurers is now closer to 95% of the item 'investment units'. +From 2001 in euro millions.

Table 11: Share of insurance enterprises in the fund inflows to specialised investment funds (estimated from the gross additions to 'units in securities special assets', after 1991 from the net additions)

		Net or gross additions to "units in securities special assets" 2) of which												
	Sales receipts specialised investment funds 1)	All insurance enterprises		Life insurance companies		Private pension and burial funds		Health insurance		Indemnity and accident insurance enterprises		Reinsurance companies	
Year	DM m (3)	DM m	% (3)	DM m	% (3)	DM m	% (3)	DM m	% (3)	DM m	% (3)	DM m	% (3)
1975	1,407	805,3	46	405,8	23	119.9	7	15.7	1	124.5	7	139.3	8
1983	3,706	2,987.6	81	1,476.2	40	720.7	20	193.9	5	384.1	10	212.7	6
1989	16,839	12,495	74	6,728	40	1,647	10	535	3	2,502	15	1,084	6
1992	23,300	10,911	46	6,829	29	822	3	658	3	1,942	8	662	3
1995	36,891	15,823	43	8,444	23	1,331	4	1,399	4	2,718	7	2,232	6
1997	107,083	43,387	40,5	25,613	23.9	4,998	4,7	3,658	3,4	4,618	4.3	4,499	4,2
1998	129,458	58,147	44,9	35,962	27.8	5,273	4,1	4,721	3,6	5,416	4.2	6,774	5,2
1999	113,152	60,208	53,2	38,624	34.1	6,308	5,6	6,113	5,4	5,173	4.6	3,989	3,5
2000	86,272	59,112	68.5	41,416	48.0	5,187	6.0	5,699	6.6	4,277	5.0	2,434	2.8
2001 *	39,015	24,729	63.4	14,379	36.9	3,668	9.4	2,753	7.0	2,615	6.7	1,339	3.4

* From 2001 in euro millions. 1) Source: Statistical supplements to the monthly reports of the Deutsche Bundesbank, Capital Market Statistics (from 1995 including money market specialised investment funds and from 2000 including fund of funds). 2) Source: Official bulletins of the Federal Supervisory office for Insurance Companies (number of reporting insurance companies not constant). 3) This assumes that four-fifths of the 'securities funds assets' relate to 'specialised investment funds up to 1992, and after 1993 it is assumed that all are specialised investment funds. 4) Statistical change after 1991: Net receipts = receipts less disposals; the later figures available from BAV annual report vary slightly (relative to size); differences in the cross totals are explicable.

Table 12: Share of securities-based specialised investment funds in total capital investments and in securities investments by type of insurance

	All insurance enterprises			Life insurance companies			Private pension and burial funds			Health insurance			Indemnity and accident insurance			Reinsurance companies		
Columns Lines 1 to 4 in DM bn	0.2 1999	0.3 2000	0.3 2001**	1.2 1999	1.3 2000	1.2 2001	2.2 1999	2.3 2000	2.3 2001	3.2 1999	3.3 2000	3.3 2001	4.2 1999	4.3 2000	4.3 2001	5.2 1999	5.3 2000	5.3 2001
Number of reporting insurance enterprises	(657)	(647)	(631)	(124)	(121)	(122)	(139 +41)	(138 +41)	(136 +40)	(54)	(52)	(52)	(256)	(253)	(248)	(43)	(42)	(41)
1) Total capital investments	1,596	1,704	943,845	987	1,056	570,947	130	138	72,039	128	142	80,953	185	188	99,468	167	180	120,438
2) Securities investments (excluding participation holding)	557	605	335,370	308	343	188,611	70	74.5	39,415	41	45.6	25,985	77.5	79	41,717	60.4	62.6	39,641
3) Securities-based investment funds*	322	381	216,335	186	227	129,186	42	47.6	27,632	22.1	30.2	17,253	40.1	44.6	25,095	28.5	31.0	17,169
4) Securities-based specialised investment funds only*	298	343	194,702	168	205	116,267	37.8	42.8	24,869	19.9	27.2	15,528	36.1	40.1	22,586	25.7	27.9	15,452
5) Line 4 as a percentage of line 1	18.13	20.11	20.63	17.02	19.38	20.36	29.08	31.10	34.52	15.61	19.12	19.18	19.55	21.34	22.71	15.41	15.5	12.83
6) Line 4 as a percentage of line 2	51.91	56.68	58.06	54.43	59.66	61.64	53.71	57.49	63.10	48.47	59.61	59.76	46.58	50.81	54.14	42.51	44.60	38.98

Note: It should be noted that the number of reporting insurance enterprises is not constant over the period. *Details about specialised investment funds alone no longer available after 1995, therefore estimated as 90% of the 'investment units' volume; in the BAV statistics, 'investment units' after 1995 means the current position of 'securities special assets', the content of which has also changed somewhat (for example, including money market fund units). **From 2001 in euro millions. Table 12 is a more detailed version of table 10.

ments are units in securities-based investment funds, of which most, in December 2001 exactly 59% (56.68%), securities-based investments were units in securities-based specialised investment funds. This further increase in specialised investment fund placements in 2001 also means that the 50% mark, passed for the first time in 1999, was no nine-day wonder, but is consistently in line with the long-term trend. Since 1999, well over half of the capital assets of the insurance companies/pension funds/death benefits funds which are generally only fund capable have been invested in specialised investment funds – which means that 'the end of the road for specialised investment fund placements' is still some way off. While it was already the case that all restricted assets could be invested exclusively in specialised investment funds, as it was only possible to invest up to 50% of restricted assets in a 'purely bond fund', up to 30% in an 'equity-based or mixed specialised investment fund', and up to 25% in a specialised real estate investment fund. Investors, however, have been slow to accept this idea. It is possible that there are still some reservations about relinquishing management of restricted assets as a whole. In this respect the specialised investment fund ITCs will have to make it their job to disperse such reservations.

❑ If the sales receipts for the year 2001 for the specialised investment funds (excluding specialised real estate investment funds) according to the Bundesbank's capital market statistics are set in relation to the corresponding net additions 'units in securities separate trust assets' or according to the new category 'investment units' with insurance companies/pension funds/death benefits funds in accordance with BAV publications, the significance of the insurance companies in the broadest sense for the securities-based specialised investment funds investment medium once again becomes evident (Table 11): just as clearly as before, in 2001 the lion's share, over 63%, of the net sales receipts of specialised investment funds was derived from the insurance companies, pension funds and death benefits funds which are subject to VAG BAV supervision;

❑ Although the flow of funds from this investor group into specialised investment funds in 2001 was almost 18% down on the previous year, it was still considerable, and constitutes the fourth highest amount going into specialised investment funds from the insurance companies/pension funds/death benefits funds in any single year to date. Not without good reason have the insurance companies already for some time been actively increasing their move into specialised investment funds business with their ITC interests, as well as from the provider side.

The strong flow of new funds into the securities-based specialised investment funds from the insurance companies/pension funds/death benefits funds investor group is also underlined by the Bundesbank statistics (Table 13), as given the different design of the Bundesbank statistics the amounts shown there, at €23.3bn, were very nearly equivalent to the €24.7bn which has flowed into specialised investment funds from the insurance companies/pension funds/death benefits funds investor group, as in Table 11.

Current values and book values of specialised investment funds of insurance companies/pension funds/death benefits funds

With the current and book values of specialised investment fund placements by the insurance companies/pension funds/death benefits funds group, we have previously had to speculate a great deal in order to bring them into line with any statements. But now there are concrete data available from the federal supervisory office for the insurance companies, as the insurance companies have to report the current values of their investments separately to the BAV, according to investment type. Chart 6 provides an overview with these earlier findings on the 'undisclosed reserves' in the insurance companies 'investment units'. According to these, the specialised investment funds' *'Réserves Occultes'* are gaining in importance, but in section B, on page 13 of its annual report for 2000, the supervisory office has added a striking paragraph concerning the publication of Undisclosed Reserves that sounds like a warning:

"Of the total undisclosed reserves, amounting to DM216.0bn (previous year: DM240.4bn), approximately 44% are attributable to real estate and to investments in affiliated companies and participatory interests. These investments are either completely non-fungible, or fungible only with considerable difficulty, but the great majority of them are commercial property for the companies' own use or group holdings. On the other hand, the undisclosed reserves in equities and investment units (51.9%, previous year: 58.1%) are very much dependent on developments in the capital markets. As this report was due to go to press (30 November 2001) it is uncertain whether the total was still as indicated."

Inclusion of securities in invested capital

In this connection too, reference must be made to the fact that for 2001 financial statements, the legislature made it possible, for the first time, for insurance companies to report their invested securities with 'invested assets'. Notwithstanding any loss of value, they were to report them in the balance sheet at the (higher) of historical or acquisition cost, provided any reduction in value is estimated as 'temporary', instead of depreciating the book value to the current market value. Credit institutions have long recognised this optional value retention right for fixed assets. They had to learn, however, that it is difficult to forecast the permanence of any loss in value. This may then lead to discussions with the auditors of the financial statements if the losses in value are considerable and if it would not be possible to present a balanced balance sheet without exercising the optional right. This optional right does, of course apply, not only to equities and bonds, but also to investment units, in particular those in specialised investment funds. In view of the investor's ability to influence the amount of a fund's annual income distribution, the particular question that then arises is the extent to which dividend-dependent reductions in value should be classified as permanent or temporary. Discussion of this question is not yet complete, but in general terms there seems to be a hardening of the view that any reduction in value, whatever the cause, must be defined as permanent if, taking into account investment policy and dividend policy there is little prospect of the unit value reaching the book value within the next four years. Independently of detailed questions of this sort, the insurance companies too now have an additional, albeit limited, possibility to exercise some sort of influence over their commercial balance sheets.

'Advisory' – between German law and EU conventions

The outsourcing issue is one in which advisory certainly plays a major role, in that investment consultancy is a widespread international business, one which in many EU States especially is treated fairly liberally – right down to the clear provisions of the Austrian law on investment funds, which in § 3 paragraph 3 states:

The investment trust company is empowered to use the services of third parties in the management of unit trust funds, and also to assign to these the right of disposal over the assets; the third party shall in this event be acting for the account of the unit holder. The investment trust company is liable for the dealings of the third party as for its own dealings.

In Germany, too, the sting has now been taken out of this issue, as the official word from the federal banking supervisory office was that the 'core business circular' of 29 September 1997 is regarded as having been practically retracted, since not even an 'empty shell' can become an investment trust company. The sector is now eagerly awaiting a circular that has been announced by the federal banking supervisory office. Until then, in the wise words of a high-ranking representative of the federal banking supervisory office (Divisional President Volckmar Bartels) in a speech in 2000, it is still the case that: "What we don't want to do under these auspices on the one hand is to weaken Germany's negotiating position in Brussels with an overly ambitious interpretation of the existing KAGG, nor on the other hand to push the investment companies into forms of organisation which in all probability will no longer be open to challenge by the law in the near or medium-term future."

Austria solution at EU level in sight

First of all, on 6.12.2001 the federal banking supervisory office (BAKred), as it then still was, published Circular No. 11/2001, entitled 'Outsourcing of operational areas to another enterprise pursuant to § 25a paragraph 2 of the Banking Act' ('Auslagerung von Bereichen auf ein anderes Unternehmen gemäß § 25a Abs. 2 KWG'). This, as expected, set out the fundamental and general rules for outsourcing. However, subsection 16 of this circular for investment trust companies includes a highly significant sentence:

"In the case of special credit institutions such as investment trust companies (Kapitalanlagegesellschaften), building societies (Bausparkassen) or mortgage banks (Hypothekenbanken) there may be certain criteria for outsourcing measures under the relevant special laws."

It may be concluded from this passage that the German Financial Supervisory Authority (Bundesanstalt für Finanzdienstleistungsaufsicht) (BAFin), or its investment department, now no longer assigned to supervising banks but to supervising securities, is planning to cancel the 'Outsourcing Circular' of 29.09.1997. This is still formally in effect, and BAFin is to replace all of it, or at least as many of its basic rules as have been superseded by the new Circular No. 11/2001, with a supplementary Circular.

In addition, since 13 February 2002, there has been UCITS III, in Article 5 g paragraph 1 of which the 'Management Company Directive', 2001/107/EC, is established as a clear framework for the delegation of activities to a fund management company (investment trust company (Kapitalanlagegesellschaft) /unit trust (Investmentgesellschaft).

"If member states permit management companies to delegate to third parties for the purpose of a more efficient conduct of the companies' business to carry out on their behalf one or more of their own functions the following preconditions have to be complied with."

There then follow nine precisely formulated provisos, and subsection 2 of the same Article goes on to say: "In no case shall the management company's and the deposi-

'Although the flow of funds from this investor group into specialised investment funds in 2001 was almost 18% down on the previous year, it was still considerable, and constitutes the fourth highest amount going into specialised investment funds from the insurance companies/pension funds/death benefits funds in any single year to date.'

Table 13: Sales receipts of domestic specialised investment funds by unit holders (excluding specialised real estate investment funds), ('regrouped' Bundesbank statistics)

	1999		2000		2001	
	in €m	in %	in €m	in %	in €m	in %
From domestic unit holders	58,000	100.25	44,464	101.64	39,339	100.8
From insurance companies (including pension funds and private retirement schemes)	24,414	42.20	24,150	55.20	23,269	59.6
From social insurance institutions + public supplementary retirement institutions	1,722	2.98	-894	-2.05	1,155	3.0
From other companies + credit institutions	29,057	50.22	18,538	42.38	12,121	31.1
(of which credit institutions)	(19,468)	(33.65)	(13,455)	(30.76)	(8,030)	(20.6)
From non-profit-making private organisations and others	2,805	4.85	2,675	6.11	2,793	7.1
From foreign unit holders	-145	-0.25	-718	-1.64	-313	-0.8
Total	**57,853**	**100.00**	**43,747**	**100.00**	**39,026**	**100.00**

Differences in totals result from rounding of figures. Source: Capital Market Statistics of the Deutsche Bundesbank and own calculations

tary's liability be affected by the fact that the management company delegated any functions to third parties, nor shall the management company delegate its functions to the extent that it becomes a letter box entity".

All of these texts, and also what we are hearing from the supervisory authorities of a number of European countries, could lead to what is being called the 'Austria solution', as quoted above, becoming standard in Europe with regard to the delegation of the right of disposal over the assets of investment companies to third parties. The branch will therefore be able to live with this, and will certainly know how to handle these new 'freedoms' in a highly responsible way.

Luxembourg specialised investment funds reach almost €42 billion fund volume

The development of specialised investment funds in Luxembourg was late in starting, 11 years ago with the enactment of the law (of 19 July 1991) relating to those collective investment institutions whose units/shares are not intended for public placement. This Luxembourg investment vehicle has now reached the substantial size of €41.7bn. It was described in detail in March 2002 on pages 263-267 of a separate study IPE (issue 6/2002).

The 4th Financial Market Promotion Act

The 4th Financial Market Promotion Act (4 FMG) came into effect on 1.7.2002, and pre-empted several issues covered by UCITS III for specialised investment fund companies. Companies with funds open to the general public are restricted to the management of investment funds and ancillary activities directly related to them, insofar as they have applied for a single EU 'passport' for each investment fund open to the general public managed by them. Pure specialised investment fund companies, however, have been able to operate as 'free asset managers' since the sixth amendment to the German Banking Act (KWG), and so, for example, they can manage a foreign securities portfolio account with a power of attorney from the owner. Now, the 4th FMG has clarified the situation, so that ITCs may also advise their clients without holding a power of attorney for the securities portfolio account.

One further innovation with regard to the permitted ancillary activities is the sale of third party funds, ie, of units in investment funds that are not managed either by the ITC itself or by ITCs that are members of the group. For specialised investment fund ITCs, however, this innovation is unlikely

Chart 6: Book values/current values/undisclosed reserves in item "investment units" for all insurance companies (excluding pension funds/death benefit funds – figures in DM m or %)

	Book values	Current values	Undisclosed reserves in DM m	as % of book value	% of total hidden reserves
12/1998 investment units	223,189	278,710	55,521	24.9	16.5
12/1999 investment units	282,187	372,799	90,612	32.1	22.4
12/2000 investment units in 2000*	300,747	362,752	62,004	20.6	28.7

*Without reassurance companies

Source: BAV annual report

to play a major role. This possibility is of interest to public ITCs, although from a literal interpretation they cannot be actively involved themselves, but have to use the services of a subsidiary or associated company without an EU 'passport'. Something to think about, however, is the conclusion that could be drawn, if 'selling' is interpreted as a preliminary stage of 'custodianship', that with such transactions unloading is unnecessary.

'Soft' funds-of-funds solutions possible

Of greater practical significance, however, is the change to § 8b KAGG, which will make it possible in future for specialised investment funds to invest 5% of their assets in inter-family security-based funds without the prior approval of the supervisory authorities. For specialised investment funds in particular, whose investment policy allows for only a small proportion of equities, or which only wish to invest a small proportion in corporate bonds, in addition to government securities and mortgage bonds (Pfandbriefe), these wishes may in future be fulfilled by the acquisition of corresponding investment funds open to the general public without formal obstacles. The commercial advantages of such a 'funds-of-funds solution' lie above all in the given risk spreading by the target funds, which cannot be so easily achieved through a direct investment in the corresponding investment segment. In this connection, however, it should be noted that a target fund would in the future also have to show a geographical or economic specialisation. There would therefore be no question of a specialised investment fund buying into an investment fund that may shift its investment goals permanently between different markets. Under the previous interpretation of the provision by the BAFin, however, it is unlikely to be assumed, in the case of an investment fund that strives for an equity portfolio that is equally spread in global terms, that that fund is sufficiently specialised. A change in this view, however, cannot be completely ruled out.

Tracker funds, relaxation of the ban on set-offs, securities lending

The pallete of possible tracker funds is being expanded. Whereas previously the only justification for exceeding the well known investment limits (5%, 10% and 40%) was the replication of a stock index on which futures contracts were traded on an official exchange, it is now possible for additional indices to be replicated where this is approved by the BAFin. So in future, for example, it will be possible to replicate the Dow Jones Index and the FAZ Index. However, under this provision, it will also be possible in future to replicate bond indices, causing the authors to wonder the replication of which bond index might possibly make it necessary for the fund manager to exceed the already mentioned investment limits.

The ban on setting off claims against the KAG with a fund's claims against the contract partner, that applied to the latter (the contract partner) is now to be relaxed so that a contract partner may now set off claims of a fund aginst him with his claims against the fund (that are legally claims against the KAG). As a result of this change, it is possible that an obstacle will be removed that may have made it difficult or impossible for some market players to conclude framework agreements for derivative-based OTC transactions, for securities lending business and for repo transactions with ITCs with effect for investment funds.

There are two areas in which securities lending will be made easier for separate trust assets. Firstly, cash balances may also be accepted in future as collateral, provided these deposits are secured. Secondly, securities lending transactions may in future also be effected beyond the date of the annual general meeting. In the past this was not permitted in the case of equities where the securities borrowers had to return the equities to the separate trust assets in time for the ITC to exercise its voting rights. In future it will be sufficient if the securities borrower hands the voting rights back to the ITC for the annual general meeting.

Rules on voting rights, 'sub-custodians', redemption fees

In the case of specialised investment funds, since 1.1.2002 voting rights have in any case been assigned to the investor. Investors must therefore add the pro rata voting rights from equities in specialised investment fund units held by them to voting rights directly owned by them, so that they can then submit the declarations as laid down in § 21 of the securities trading law (WpHG). In practice, however, there are hardly any specialised investment fund investors for whom this new rule is likely to have any consequences, as for example about €150m would be required before the lowest reporting limit of 5% was reached, even for the smallest DAX security.

Whereas previously the depositary bank at least had to hold domestic securities in its own custody, in future it will also be permissible to use the services of other domestic depositaries as sub-custodians. As with foreign securities held in custody by a custodian bank in the respective country, the depositary bank may also limit its liability for any errors made by such a 'sub-custodian' to what is known as 'culpa in eligendo', or fault through its poor choice of servant (prevailing management practice).

The licensing of redemption fees does not just make it possible for investment funds open to the general public to be differently structured. Specialised investment fund companies may also, by agreeing a contingent redemption fee, safeguard itself against financial loss in the event of a new client wishing to cancel a specialised investment fund within a short time of its issue.

Licensing of unit classes

The possibility of offering the same fund through different unit classes could be of huge significance for specialised investment funds. Up to now, the so-called multi-investor specialised investment fund, or specialised investment funds with more than one investor, could only be issued under special circumstances, as neither the investment policy nor the dividend policy could be tailored to the special requirements of each individual investor. With the new unit classes, it will in future be possible to tailor at least the dividend policy individually to the requirements of each individual investor. The popularity of mutual funds could increase significantly in future if, under IAS regulations, 'one-investor funds' actually have to be fully consolidated on the consolidated balance sheet, something that would naturally affect the so-called 'corporate' specialised investment funds. Unit classes would then at least obviate the problem of the uniform dividend policy. Unit classes, however, would have a uniform investment policy, as this would not be a completely separate investment fund, as is the case with the different subfunds of an umbrella fund. The unit classes could, for instance, be distinguished only by their dividend policy, the amount of the management fee, the front-end load and the currency of the unit value.

The 4th FMG has not yet brought about the long-expected merging of investment funds. Even if this proposal had been implemented in the KAGG, any mergers would have resulted in the fiscal realisation of undisclosed reserves. So it has been left to future legislative planning to find a solution for this.

The task to find out the correct unit price will no longer be attributed exclusively to the depository bank, but now this can also be done by the ITC. In practical terms, part of this change to the law means little in the way of major innovation, as even before the change there were a few depositary banks that calculated that ascertained the unit price by investigating this figure through requests to the ITC. On the other hand, this change to the law will certainly mean a cost saving in a few cases, if each individual depositary bank – and there are certainly more depositary banks than ITCs – no longer has to calculate unit values itself, but can instead concentrate this activity on the ITC.

Conclusion

Despite the downturn in volumes among securities-based/fund of funds specialised investment funds caused by developments on the global capital markets, net receipts in 2001 remained at a remarkably high level, at €41.3bn. Fund numbers also rose over the past year (by 2.1%). It was only in the first few months of the current year that a certain wait-and-see attitude became prevalent with regard to specialised investment funds, which did not, however, affect specialised real estate investment funds. The reason for the cautionary approach in this current year could lie in the fact that people want first to familiarise themselves with the latest legal reforms (Investment Directive, 4th FMG), because in the medium to longer term, the specialised investment fund has in many respects lost none of its attractiveness as the optimal investment vehicle: on the contrary, in many of the new regulations there are genuine incentives for investing in specialised investment funds.

This report was published earlier this summer in German in Zeitschrift für das gesamte Kreditwesen No 15/2002, by Frankfurt-based Fritz Knapp Verlag

This study was completed as at June 15, with the available figures as at end of March. In the meantime, specialised investment fund figures are available up to end of May. It is true that in April funds grew more strongly again, but in May the market was again weaker regarding fund numbers, net receipts and volume, so that the comments made about the first quarter and the need for a 'wait-and-see-attitude' still hold good.