BF BETTER FINANCE
The European Federation of Investors and Financial Services Users
Fédération Européenne des Épargnants et Usagers des Services Financiers

PRESS RELEASE

EC proposal to amend Solvency II Equity Calibrations: an opportunity to return to well-performing long-term life insurance products:

Solvency II equity-to-own funds calibrations to be reduced to 22% in some cases to support long-term investments.

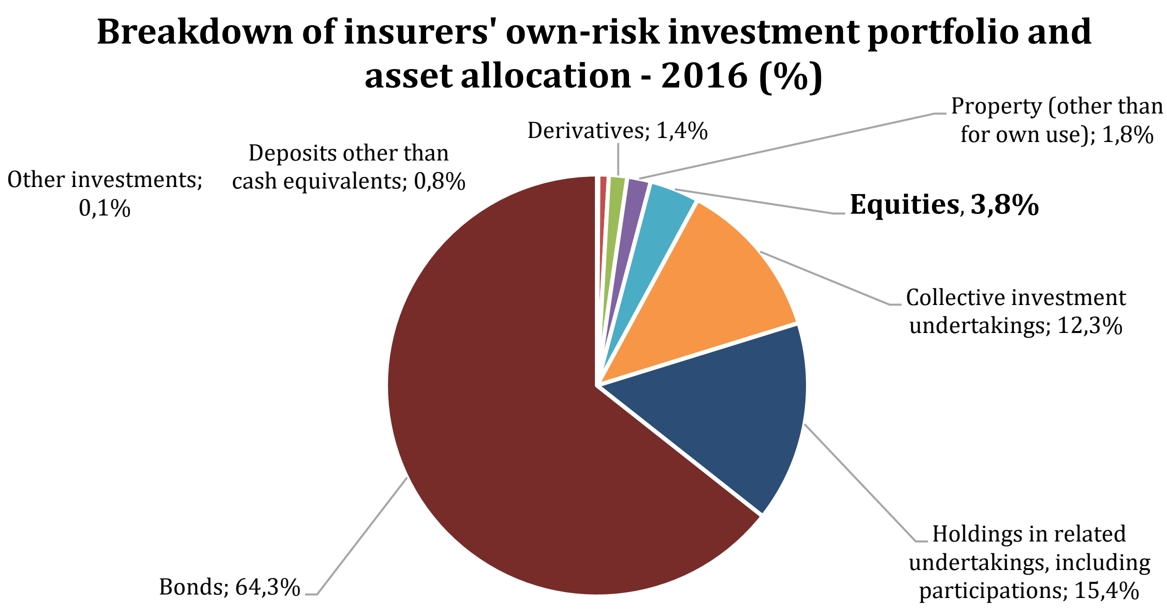
12 November 2018 – BETTER FINANCE's (and others') unabated efforts to convince the EU Authorities to recalibrate the capital requirements for equity have started to bear fruit.

On 9 November 2018, with the input of BETTER FINANCE and other stakeholders, the Commission tabled targeted amendments to the Solvency II delegated regulation, in particular to the equity calibration. The amendment creates a derogatory provision for "long-term strategic investments in equity", for which the capital requirement (SCR) is smaller. Such a provision would ensure that the capital requirement for a stock that qualifies for the abovementioned category would only be of 0.22€ for each stock worth €1.

The so-called Solvency Capital Requirement (SCR) is a ratio determining the amount insurers need to keep as capital for each euro invested in capital markets. This ratio is meant to ensure that an insurer's technical provisions are sufficient to cover future liabilities over a 12-month period in case a certain situation results in losses. Basically, it guarantees that the company has the capacity to absorb losses without altering the claims of policy holders.

In the calculation of the SCR, special attention is given to equity investments, which are considered riskier. Up to now, the Solvency II Regulation and the implementing acts provided that insurers must set aside 0.39€ and 0.49€ respectively for each 1€ invested in listed and private equity. In other words, buying a 1€ share costs the insurer 1.39€/1.49€.

This is detrimental to both insurers and long-term and pension policyholders, since the long-term return to policy holders is tied to the performance of the actual investments. But with very low equity investments over the past 14 years, one cannot expect good long-term net real returns.



Source: Insurance Europe, European Insurance Industry Database (last updated 30 October 2018)

In several public consultations and requests for evidence from the European Commission, BETTER FINANCE pointed out that long-term investments in equity are much less volatile than on a 12-month period and should require less capital.

In stark contrast, investments in Eurozone sovereign bonds have a 0€ capital requirement, which in theory would make them absolutely risk-free. What's more is that the monetary policies of Central Banks across the EU generate ultra-low interest rates - and sometimes negative ones – on these bonds, resulting in "financial repression" with long-term returns all too often entering negative territory in real terms (after inflation).

BETTER FINANCE welcomes this proposal as a first step to stop penalising insurers for investing in equities to cover their long-term and pension liabilities. We hope, though, that the EU Parliament and Council will alleviate the multiple constraints that still severely hamper the EC proposal.

Read the European Commission's proposal here.

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Contact: Chief Communications Officer | Arnaud Houdmont | +32 (0)2 514 37 77 | houdmont@betterfinance.eu