

To: Solvency II WG  
From: Prudential Team  
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Subject: EIOPA's Financial Stability Report June 2024

## Background

On June 27 EIOPA published its Financial Stability Report. This report provides an overview of significant developments and risks within Europe's insurance and occupational pensions sectors.

Please find below a summary of the report prepared by the secretariat. The link to the full report is [here](#) for those who wish to read it in detail.

## Summary

### Key Developments

- Geopolitical tensions, including the ongoing conflicts in Ukraine and the Middle East, are contributing to market and inflation risks. Also the upcoming elections add to global economic uncertainties.
- The euro area's economy experienced a modest improvement at the beginning of 2024 relative to late 2023, though overall activity is anticipated to stay low. Average global GDP forecasts show slight improvement.
- In financial markets, interest rates peaked in Q3 2023 with expectations of future rate cuts. Yields of sovereign bonds have decreased, while spreads have narrowed and equity markets seem to perform strongly.
- Many natural disasters happened in 2023, appearing worldwide high insured losses estimated at € 86,0-97,7 bn. Especially in Europe, we experienced severe thunderstorms and flooding which only that amounted to € 7,2 bn insured losses.

### Cyber risks and digitalization

- The threat landscape for cyber risks continues to expand. The frequency of cyber incidents varies across the EEA, with an overall increase noted. Supervisors are closely monitoring cyber underwriting and the associated operational risks. Cyber underwriting remains limited due to pricing challenges and uncertainty about the nature of these risks.
- Digitalization introduces both opportunities and risks for the insurance sector. Insurers are adopting new technologies in underwriting, claims, and operational management. However, those failing to adapt face the risk of losing premium income. Digital operational resilience remains a priority, supported by initiatives such as DORA, the Artificial Intelligence Act and the ESAP.

### Alternative assets and real estate

- To navigate the prolonged period of low interest rates many insurers (*especially life ones*) have turned to higher-yielding but riskier investments, known as alternative assets. EIOPA note that these assets are complex, less liquid and include private equity, private debt, real estate and infrastructure investments. In Q4 2023, insurers demonstrate still a significant allocation to alternative assets, comprising 16,0% of their investments with the real estate exposure to stand out as a prominent allocation.

- In the report, EIOPA notes that there are several supervisory concerns characterising alternative investments including valuation, liquidity, macroeconomic environment and credit risk. It concludes that insurers' exposures towards private credit/debt must be closely monitored by regulators and supervisors.
- Insurers' exposure to real estate related investments increased from 7,3% at the introduction of Solvency II to 9,9% of total investments by Q4 2023. Since fluctuations in the real estate market directly affect the value of these investments, EIOPA emphasizes that the correlation of the real estate market with the financial system poses systemic risks, necessitating regulatory oversight to ensure financial stability and mitigate potential threats.

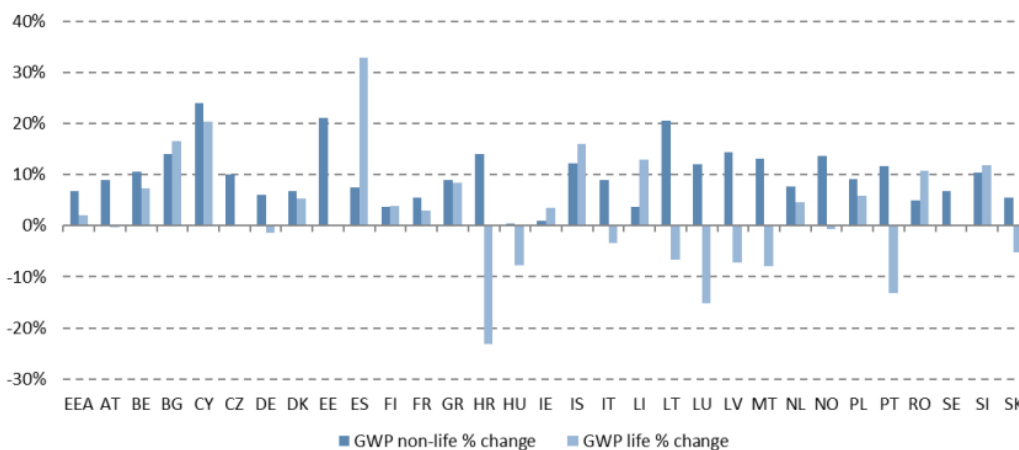
#### Crypto assets

- Crypto assets serve as both direct investments by insurers and indirect investments through unit-linked products for customers. Policyholders can also use crypto assets for paying premiums and claims on traditional insurance policies. However, as of 2023, crypto assets comprise only 0,02% of total assets under management in the insurance sector.
- Regulatory responses to crypto assets emphasize risk-based approaches under principles like "same activities, same risks, same rules". The Markets in Crypto-Assets Regulation (MiCAR) establishes unified rules across the EU for specific types of crypto-assets. Similarly, new initiatives to adapt the prudential regime applicable to insurance undertakings to consider crypto assets' risks are being launched in the context of the Solvency II 2020 review.

#### European Insurance Sector

- Regarding the insurance companies' capital, the median SCR ratios improved in Q4 2023. More specifically:
  - Life sector – 243% (up from 232% in Q4 2022)
  - Composite – 225% (up from 207%)
  - Non-life sector – stable at 215%
- An improvement in profitability was shown due to higher returns in investment portfolios among higher interest rates. Also the median ROA and the median return on excess of assets over liabilities improved as well.
- The GWP in non-life insurers continued to grow due to rising claims costs and inflation adjustments. On the other hand, life insurers saw a moderate increase but with varied trends across Member States (some countries experienced a large growth, when others a reduction). Lastly, the share of unit-linked business decreased to around 34,2% at the end of 2023.

**Figure 2.1: Total Life and Non-Life GWP growth from 2022 to 2023 (in %, year-on-year)**



Source: EIOPA Quarterly Reporting Solo. Note: EEA weighted average. Growth rates are computed by weighting the GWP per reporting currencies.

- From a prudential perspective, EIOPA highlights the importance of catastrophe modelling tools and data provision for effectively managing climate risks. They also state that sustainability risks are crucial for the future viability of insurers. Additionally, EIOPA is preparing for the implementation of the revised SII Directive and aiding in the finalization of the ICS.

#### European Reinsurance sector

- The European reinsurance sector performed well in 2023, benefiting from hardening market conditions. Reinsurers increased their written premiums, improved underwriting performance and sustained strong solvency positions. The median solvency ratio was around 223,4% at the end of 2023.
- GWP for non-life reinsurance increased in 2023, while life reinsurance premiums declined. Reinsurance GWP covered 18,0% of the total GWP in the EEA sector in 2023, with non-life reinsurance representing 13,9% (€190.8 bn) and life reinsurance accounting for 4,1% (€ 56 bn). Moreover, the profitability of non-proportional reinsurance improved significantly, driven by a 4.8% drop in incurred claims and a 16.4% increase in earned premium in the property line of business.

The report lastly examines the gap in pensions between genders looking at labour market structures, pay gaps, and investment behaviours. Additionally, it suggests ways to improve pension outcomes for women.