Insurance Europe comments to the Capital Markets Union Consultation by LE Europe on the creation of a CMU dashboard

Referring to: LE questionnaire on the creation of a CMU dashboard

Life Insurance Questions of the LE Europe survey related to the study on the creation of a dashboard of indicators to monitor the development of the Capital Markets Union (CMU).

1. What factors, related to capital markets, are most important for investment in infrastructure (e.g. the growth of ELTIFs, the backing of government institutions, e.g. EIB)?

The economic factors identified by LE (such as diversification of investor base, consistency of infrastructure investment, availability and standardisation of sustainability data) appear to be suitable in principle. However, the **economically important factors** for investments in infrastructure should be supplemented by the following factors:

1. Number and availability of **suitable infrastructure and sustainable assets for private investors.**
2. Increased involvement and **no crowding-out of private investors by supranational development institutions.**
3. Availability and standardisation of **infrastructure project data.**
4. **Support of private investments with appropriate measures**, such as credit enhancements from supranational development institutions.

Other key factors that determine for investment in infrastructure are effective regulatory frameworks, notably investment and prudential regulations. Institutional investor regulations (pension and insurance) might represent unintended barriers to long-term investments, exacerbating the lack of suitable project pipelines, investment cost requirements, and poor risk-assessment frameworks. Therefore, policy and regulatory reviews should focus on identifying these barriers, while balancing the need to protect beneficiaries and supporting appropriate risk management arrangements.

Focusing on prudential regulation, Solvency II is a key factor affecting insurers' investment allocation, including in infrastructure. The ability to make long-term investment in assets such as infrastructure is given by the flow of premiums from long-term business such as pensions and saving. Solvency II should therefore be calibrated in a way that safeguards the viability of long-term products that generate long-term investments. The current extrapolation method is a key component which already serves for this purpose and needs to be preserved. Besides, Solvency II needs targeted improvements to better reflect the true risks and economics of insurers' long-term business model. In practice, this means improving the measurement of both available capital (by both reducing the level and volatility of the Risk Margin and improving the Volatility Adjustment mechanism) and required capital for investments (this includes improving the criteria for long-term equity and the calibration for corporate debt). The ongoing review of the Solvency II framework should focus on assessing concerns related to long-term business and long-term investment. Addressing the flaws of the framework will remove barriers and lead to more capacity for long-term investment, including in infrastructure.

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2. What indicators can be used to measure the factors that you have suggested?

Possible Indicators could be:

1. Number and availability of **suitable infrastructure and sustainable assets**:
   - Investment flow from insurers into infrastructure investments
   - Scope of a project pipeline
   - Standardization of investment processes and investment opportunities
2. **Increased involvement of private investors**:
   - Percentage of infrastructure financing with participation of private investors
   - Limitation of development institutions to projects that otherwise could not be financed at market conditions.
3. Availability and standardisation of **infrastructure project data**:
   - Degree of standardization of infrastructure projects
   - Access and availability of project data for private investors
4. **Support of private investments with appropriate measures:**
   - Number of projects that cannot be realised by private investors without the support of development banks such as credit enhancements.

The collaboration of governments with private sector investors at early stages of project development can help better define the role of private sector investors and improve appropriate risk management practices to facilitate infrastructure investment. Therefore, Insurance Europe suggests that indicators try to capture the engagement of risk management experts (ie supranational development institutions, insurers) from the early stages of project development. This will help minimise the project cost and build confidence in projects from investors.

Regarding regulatory impact, this measurement is hard to disentangle from other factors. This is why key indicators should focus on the effect of policy changes in Solvency II as outlined in the response to question 5. In addition, indicators of insurers' investments in key asset classes should also be monitored.

3. What factors are most important for development and integration of the green bonds market (e.g. the development of a European green bonds framework)?

A number of factors are key for development and integration of the green bonds market. In particular, the insurance sector highlights the following factors:

- a **limited supply of green projects to be financed by green bonds,** which is in fact unable to meet the growing demand of investors to invest in attractive green assets
- **the additional costs, expertise and internal resources** to analyse the issuer's dedicated information and reporting, including the use of proceeds, (especially in the absence of external review procedures)
- the **risks related to greenwashing**, especially in the absence of a sustainability taxonomy - sustainability has different meanings to investors across markets, and currently there is not common understanding of what is sustainable. A clear understanding is key to encourage insurers to invest with confidence in green assets, eg by significantly reducing reputational risks, and further contribute to the sustainability transition.
- inconsistent **and/or incomparable ESG data,** which hinder the implementation of ESG strategies by institutional investors, especially for large and diversified investment portfolios
- the **lack of harmonisation in standards, definitions and market practices** which negatively impacts the comparability of green bonds.

From an issuer perspective, clear economic benefits and additional concerns with reputation are also relevant factors that affect the market development

4. What indicators can be used to measure the factors that you have suggested?

The main indicators should focus on green bond issuances, including amount of new issued green bonds and the general **market share of green bonds**. Equally important, it is key to monitor progress not only from private investors, but also from government. In this respect, the insurance sector recommends monitoring the issuance of **sovereign green bonds**.

Another indicator, related to the market development, is the **share of bonds using the newly set up EU Green Bond Standard**, as this is expected to facilitate issuance and lower issuance costs as well as risks related to reputation and greenwashing. In terms of information and data, the **availability of standardised information at issuer level** would also be important.

Due to the abovementioned factors, a growing demand from investors and a limited supply of green projects to be financed by green bonds, it can happen that the issuance of a green bond leads to lower expected returns in comparison with that of bonds with similar characteristics. Therefore, the risk-return ratio of green bonds (especially those using the newly set up EU Green Bond Standard) could be carefully monitored as a further indicator for the development of the green bonds market.

5. What factors are most important for the development and integration of a green investment fund market (e.g. investor demand for green investment products)?

The development and integration of a green investment fund market is affected by similar factors as those highlighted in question 5. In addition to the above-mentioned factors, the development of a green investment fund market appears to be affected by:

- **the lack of suitable sustainable investments**. As already described above, the demand for attractive sustainable assets is not matched by the availability of such assets. It is crucial that the right incentives are in place to stimulate the transformation to a more sustainable economy, which will lead to increases in the volume of "green" investments.
- **the lack of sustainability data**, especially for individual companies' activities and for each funding instruments. Sustainability data for each actual and potential investment is necessary for investors:
  - to apply a sustainable investing approach and to draw comparisons across companies
  - to comply with upcoming disclosure requirements.

  If ESG information is unavailable, poorly standardise or inaccurate, then it is more complicated for insurers to fully integrate ESG into their investment processes and disclose relevant information on their investments. Most importantly, with thousands of financial actors investing in thousands of different investments, each investor would have to do their own sustainability assessment for each investment. This would be very inefficient and would lead to inconsistent results with different investors arriving at different assessments for the same investment. To address this issue, European insurers note that a centralised EU database/register should be set up to collect ESG data in a standardised and ready to use format, including information based on the EU environmental taxonomy.
- **the lack of ESG assessment for sovereign bonds and related competitive distortions at investment product offering level**. Life insurers' participation to the green investment market is negatively affected by the existence of competitive distortions compared with other financial market participants offering fund-like products. Specifically, insurers usually invest in a broad mix of products (eg corporate bonds, covered bonds, government bonds, equities, real estate, mortgages, infrastructure, etc), which is reflected in the composition of the investment products that they offer. However, achieving a high sustainability degree for this complex mix of asset classes, especially for sovereign bonds as key component of the portfolio, is challenging considering the currently limited supply of sustainable assets. Therefore, green insurance products that include a substantial share of government bonds (eg linked to a guarantee) would not be able to successfully compete on environmental grounds against other fund-like products that can more easily achieve full environmental sustainability. For example, this is observable in the context of the EU Ecolabel, which currently penalises guarantee-based products from its scope.

6. Are there any other factors which are relevant to infrastructure and sustainable investment markets? How can these factors be measured?

Insurance Europe notes that long-term investors as insurance companies benefit from stable and reliable investments infrastructure and sustainable investment frameworks. Continuity and stability over time of investment policies and framework, including disclosure frameworks and taxonomies, have positive effects on investors' confidence, potentially contributing to higher investment levels.

LE Europe's preliminary work has identified several factors relating to infrastructure investment and sustainable investment, and indicators to measure these factors. The table below lists indicators which can be used to measure factors in the left-hand side boxes.

Economic Factor	Indicator
Diversification of the investor base	Proportion of infrastructure investment from pension and life insurance funds
Consistency of infrastructure investment	Number of ELTIFs (European Long-Term Investment Funds) Investment flows into ELTIFs
Availability and standardisation of sustainability data	Proportion of sustainable investment vehicles with an EU-approved label (contingent on development of the label)
Investor demand for green investment products	Proportion of pension funds / life insurers with a mandate to invest in sustainable products

7. Are there any indicators which do not accurately measure the factors in the boxes? For example, is the consistency of regulation accurately captured by the growth of ELTIFs (European Long-Term Investment Funds), or are other aspects of regulatory consistency important?

With regard to the Economic Factor "Consistency of infrastructure investment" proposed by LE, the sector notes that the number of ELTIFs is not a meaningful indicator of consistent investment in infrastructure. There is a wide range of investment opportunities (direct/indirect) in infrastructure and ELTIFs are only of minor importance for infrastructure investments by insurers. Rather, a meaningful indicator would be the number of suitable available projects and the investment flows of insurers (direct/indirect) into infrastructure projects.

8. Are you aware of any alternative indicators that measure the factors in the boxes more accurately? If so, what are these indicators?

A good indicator could be the investment share allocated to private investors within defined investment plans or the increase in infrastructure investment within existing or planned investment projects by the private sector.

9. Are you aware of any data sources that might contain any useful indicators? If so, what are these data sources? For example, official statistics, proprietary databases, administrative / regulatory data, EU-wide sources, national sources, third country sources.

Most infrastructure-related data sources do not fully capture the performance of infrastructure investment across financial dimensions, sustainability and geographies, often due to confidentiality reasons or poorly data collection design and harmonisation. In this respect, it would be useful if supranational development institutions could collaborate to build reliable data sets to be shared with the private sector.