Key messages on the future of the CMU

The European insurance industry believes the Capital Markets Union (CMU) project should focus on three key objectives in order increase prosperity for EU citizens, stimulate growth, innovation and competitiveness for EU businesses and to meet the EU's massive needs for climate, digital and other investment. In particular, delivering on these objectives will help ensure the private sector can play its role in financing the green transition as well as European venture capital, SMEs, infrastructure and listed companies thereby ensuring growth and jobs, and paving the way for a financially and economically stronger Europe.

The three objectives are **increasing retail investment**, **diversifying sources of funding for EU businesses** and creating a conducive **environment for EU companies (start-ups, SMEs, listed companies) to innovate, compete and grow.**

This paper highlights key actions for achieving these objectives, including those that would allow the insurance sector to significantly increase its contribution.

The European insurance sector contribution to achieving the CMU objectives

Providing protection to EU citizens and businesses

Insurers provide financial protection to citizens and businesses in the event of adverse events and offer mechanisms to manage, mitigate and cope with the risks they face, thus reducing hardship and playing a key role in supporting the resilience businesses need to conduct their activities and grow.

Insurance products boost retail participation in capital markets and help tackle demographic challenges

Insurers play a very significant role in the provision of pension and savings across the EU. They provide retirement savings products, occupational pension and insurance-based investment products (IBIPs) in fact they represent the largest portion of retail investment in Europe (70%[1]), thus having a crucial role in the development of the CMU.

They are the only products that can help retail customers invest long-term, prepare for old age, and at the same time provide them with safety due to additional features and benefits. These include financial guarantees and coverage against a variety of biometric risks, such as longevity, death, hospitalisation, inability to work or unemployment - elements that many consumers value and look for, and are key to their investment decisions. Insurers offer a variety of products enabling people with different risk profiles to invest in capital markets. This includes products with high levels of safety, through profit-sharing and guaranteed products, insurers serve the needs of the many small savers who would otherwise not have the confidence to invest at all due to fear of losing their money.

Insurance savings products are available to retail investors through multiple distribution channels, like agents, brokers, bancassurance, or directly through insurance companies themselves. Having a wide choice of distribution allows consumers to have broad access to investment.

One of the largest long-term institutional investors

The insurance industry is one of Europe's largest institutional investors and an important provider of stable, long-term funding for governments and businesses. Insurers are uniquely positioned to contribute to sustainable economic growth and to help finance digitalisation and transition to a carbon-neutral, more sustainable and resilient economy. European insurers invest close to €9.5 tn in the economy and 69%[2] of their

[1] 2021 EIOPA estimates.

[2] EIOPA estimates (link)

investments in equity, corporate and sovereign bonds are within the EU. Investing is a consequence of the insurance business model: policyholders pay premiums upfront, which insurers then invest to meet future claims and benefits. Insurers' business model allows them to have a long-term investment time horizon, to focus on the long-term performance of assets, invest in illiquid assets and to act as a countercyclical buffer. These advantages benefit the economy and also allow insurers to better invest for the benefit of their customers, thereby contributing to reducing the pension gap.

Current challenges

Today, EU businesses and citizens are not able to benefit from the deep, diversified, efficient and secure funding and investment and EU businesses are not growing at the same rate as in other global markets. To change this, a number of challenges need to be tackled:

To increase retail investment…

While the EU has one of the highest saving rates in the world, it is marked by a very low level of retail investor participation in capital markets – a 2022 study[3] showed that 72% of citizens were not investing in any financial product. The EU thus needs to encourage increased retail participation in capital markets. However, there are behavioural, practical and regulatory barriers that need to be overcome. For instance, many Europeans under-estimate their need to invest for retirement; they often lack the confidence, knowledge or interest in directly investing in the capital markets. Many Europeans also tend to be highly concerned about the safety of their savings and the risks of investing directly. As many have limited resources and ability to withstand losses, this concern is understandable. The importance of this is confirmed in Insurance Europe's Pan-European Pension Survey[4] where by far the highest priority was the safety of the money invested.

Another barrier to investing is the fact that potential investors can be put off by the overload of (complex) information providers are required to give them and by the long and un-appealing process they are required to go through.

To diversify funding for EU businesses…

The reliance on banks for funding, and more generally, the lack of diversity in funding sources for EU businesses is a well-known issue and a key focus of the original CMU project.

There are various drivers for this situation, and in particular, preventing insurers from playing a bigger role. One of them is excessive regulatory capital charges insurers are currently subject to including those applying to equity investments. The industry has long highlighted that the capital charges for insurers should better take into account the long-term nature of the industry and how this impacts the real risks they face. In the case of equities this means basing capital charges on the risk of long-term underperformance of the asset and not only on a short-term trading risk approach. This would lead to more appropriate, generally lower capital charges, and enable insurers to invest more.

Another current barrier is that CMU type assets (European private debt, private equity, venture capital, listed equity, infrastructure) can be hard for insurers to access due to lack of sufficient scale and lack of suitable information on those assets,

Also, insurers' cross-border investment can be limited by the lack of harmonisation of insolvency proceedings and the lack of clear dispute settlement procedures between investors and member states.

[3] "Disclosures, suitability and inducements", Kantar study, 2022 (link)

[4] Covering 16,000 people across 15 countries (link)

To a create conducive environment for EU companies (start-ups, SMEs, listed companies) to innovate, compete globally and grow…

The EU rightfully has high ambitions to create a strong regulatory framework to protect citizens, the environment and enhance financial stability. However, it tends to create overly complicated, overly detailed and overlapping regulation. As a result, the EU regulation applicable to businesses operating in Europe is tying up significant costs and resources, limiting their ability to innovate and grow and reducing Europe's global competitiveness. It impacts all European companies but can be particularly overwhelming for start-ups and SMEs.

Recommendations

The insurance industry recommends the following actions under the scope of a renewed capital markets union project to address these challenges and help increase retail savings, diversifying funding for EU businesses and create an environment for EU companies to grow.

To increase retail investment…

Increasing the flow of money into savings and retirement savings is key to increasing the funds available for the investment by institutional investors, including insurers. It will also increase the financial wealth and resilience of the citizens investing and so help close the retirement savings gap. Private pensions saving should be encouraged, Pension Tracking Systems (PTS) should be promoted and if the PEPP is to play a role, the PEPP Regulation should be fundamentally revised and simplified.

Make it easier for consumers to invest in savings and pension products

The Retail Investment Strategy (RIS) needs to be used to encourage and facilitate savings, while ensuring consumers remain protected from bad practices. This means reducing and not adding to the current information overload and complicated, lengthy sales process that discourage EU citizens from investing. It means making full use of the help digitisation can provide in simplifying and streamlining the process. The RIS should not limit existing access to advice and distribution channels as this would reduce and not increase savings.

Improve prudential rules which act as barriers

The Solvency II Review needs to deliver on its potential to address the Solvency II framework's current excessive capital and volatility, resulting in unnecessary barriers for long-term, guaranteed and profit-sharing products.

Improve financial and insurance education and nudging mechanisms

Efforts at EU and member state level to promote financial and insurance education have a vital role to play in ensuring that European citizens are equipped with the knowledge, confidence and skills necessary to improve their understanding of financial products. Pension dashboard and tracking systems can nudge and help citizens to invest more.

To diversify funding for EU businesses…

Insurers already invest significant amounts in EU equity markets but reducing certain barriers would enable insurers not only to invest more in equity, but also to increase significantly their investment in assets that are currently difficult for them to access such as venture capital, SME equity and debt, and infrastructure.

Improve prudential rules which are unnecessarily holding back insurers' investments

Improvements targeted at improving capital requirements for listed equities are under discussion as part of the Solvency II Review. However, other areas of the review, aimed at reducing excessive overall capital and volatility also have a major impact on the capacity of insurers to invest. It is therefore key that the Level 2 technical details of the Solvency II review are finalised taking into account the impact of the review on the fulfilment of the CMU objectives.

Increase insurers' access to SME equity, venture capital, SME debt and infrastructure

There are examples at national level of funds[5] being created, often with the involvement of insurers and governments, containing SME equity and debt, venture capital or infrastructure assets. Such funds provide the scale and access for a wide range of insurers to invest in these asset classes. Actions should be taken to assess where and why such funds have been successful and how their use can be expanded to other EU markets. The potential for multi-national or EU versions of such funds and potential benefits involving financial instruments such as Invest EU should be investigated.

Facilitate greater cross-border investment

Increase trust and confidence in cross-border investment within the EU, by making progress in the areas of insolvency law and increasing intra-EU investment protection. Harmonising creditor rights and the legal status and powers of insolvency administrators to trace assets belonging to the insolvency estate would help to ensure that the interests of creditors are appropriately considered and thus contribute to more confidence in a fair liquidation and reorganisation process. To increase the intra-EU investment protection a straightforward process for settling or deciding disputes between investors and Member States should be implemented.

To create a conducive environment for EU companies (start-ups, SMEs, listed companies) to innovate, compete globally and grow…

Reduce the EU regulatory overload

Europe needs to change its approach to regulation to reduce the regulatory overload that is stifling EU innovation, growth and global competitiveness. Firstly, this means the European Commission delivering on its commitment to reduce existing regulatory reporting by 25%.

Secondly, for new regulation, it means changing the current policy making culture and developing and enforcing clear principles of good, efficient and effective regulation. In this way new regulation would be introduced only when truly needed and be simpler, proportionate, avoid unintended consequences and be focused on achieving meaningful progress rather than perfection.