# Listed property's solvency boost

Changes to Solvency II should result in more money flowing to equities. **Paul Strohm** reports

Changes to the European Solvency II regulations that came into force earlier this month (8 June) have reduced the capital requirement for insurance companies holding equities from 39% to 22%.

The level now compares favourably with the 25% requirement for direct holdings in property.

The Brussels-based European Public Real Estate Association (EPRA) has been campaigning since Solvency II came into force in 2016 to get the capital requirement reduced for holding equities.

EPRA's director of public affairs, Tobias Steinmann, told *EuroProperty* that the amendment marks 'significant progress for listed real estate and is a strong step in a move to have the asset class treated fairly by regulators as a long-term investment'.

He added: 'Having the solvency capital requirements now almost halved to 22% will make our sector more attractive to investors.'

REITs and quoted companies are now thought likely to be in more demand given the increased scope insurance companies will have for investment in equities. Any increased investment volume could particularly benefit those property companies and REITs whose shares trade at a discount to their net asset value (NAV).

Before this month's amendment to the regime, EPRA had said it was concerned that the Solvency II rules were hindering insurer investments in listed real estate. At 39% the industry had one of the highest Solvency Capital Requirements (SCR) for equities. In contrast, direct real estate was treated with what EPRA regarded as a preferential SCR of 25%.

The association said that among its members are some of the largest European insurance companies which had argued that the SCR for listed real estate, being part of the equity category with a 39% SCR, had hindered investment 'into the stability and growth the sector provides'.

EPRA had sought to distinguish property equities from other share sectors, arguing that institutional investors such as insurance companies invest in real estate shares as part of their long-term investment allocation. And it had argued that as a consequence of the Solvency II rules, insurance companies were forced to invest in real estate either directly or 'through more opaque investment funds'.

The association said the result was a higher concentration of assets and lower liquidity, and that investment was not flowing into real estate through the more open, transparent and liquid channels.

## REIT UP FOR SALE

The changes would appear to have been made too late for Dublin-based Green REIT, which has put itself or its assets up for sale after only five years' trading and has attributed this, at least in part, to Solvency II.

In April Green, one of only three listed REITs in the Irish property market, began the sales process because 'the company's share price has been subject to a material and persistent structural discount to its net asset value per share for over three years'.

When the market closed on Friday 12 April before the sales announcement was made, the discount was 17%, with the shares trading at €1.52 against half-year NAV of €1.83 at 31 December 2018.

This week Green declined to comment as its sale process is in train. However, in several conversations with EuroProperty prior to the sales announcement, CEO Pat Gunne had said: 'We are up to almost €1.5 bn gross assets, €1.3 bn of equity, and annualised contracted rent roll of €75m showing a yield at portfolio level of about 5%.'

'So we're delighted with that. And yet, every meeting is ending up with: what's the story on the discount?'

He said Solvency II regulations made investing in listed property more onerous than in direct assets. 'The volume of capital on the direct side is staggering. Our stock is very institutional – European pension funds should be holding it.'

Although EPRA has welcomed this month's change, Steinmann said there is still more work to be done and EPRA wants to get the holding period necessary for shares to qualify as 'long term' reduced.

He said: 'The rules apply to a sub-category for "long-term investments in equities", with a minimum holding period of five years.' He says this is too long and that the insurance industry should be allowed more agility, notwithstanding its long-term perspective.

John Forbes, of John Forbes Consulting, said the changes need to go further and added that the conditions for achieving the lower capital charge are very complex. 'My view is that this makes it not very useful unless things change dramatically. I have not met many insurers who are very excited by this. The volatility adjustment on each investment cannot be looked at in isolation.

'Correlation also needs to be considered, so taking the position that investment in REITs should be regarded as listed equities rather than real estate could be a double-edged sword.'

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**Tobias Steinmann, EPRA**