

November 2026

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Unlocking Private Equity Under Solvency II

Revised Solvency II framework opens up the opportunity for greater private equity investment

European insurance companies will be able to access private equity investment on far more capital-efficient terms from January next year under the European Union's revised Solvency II framework.

The revision, which comes into force from January 30, 2027, essentially clarifies eligibility for long-term equity investment (LTEI) treatment by removing the ambiguity that has long limited insurer's access to the framework's favourable 22% capital charge.

The ambiguity primarily stemmed from the stringent, open-to-interpretation eligibility criteria, including mandating that an LTEI portfolio be identified and managed separately from other activities, and insurers needing to demonstrate they would not be forced to liquidate their equities under stress.

With clearer rules under the revised framework, insurers will be more confidently able to classify suitable equity holdings as LTEIs, potentially unlocking greater and more efficient private equity investment across differing strategies.

The regulatory change comes as part of broader reform of the Solvency II regime, which we recently analysed in our piece *Solvency II Reform: Implications for Asset Allocation and ALM*.

In this paper, we summarise the upcoming regulatory revision and highlight key considerations for implementation.

Qualitative Requirements

Insurers can treat some of their equity investments as LTEIs if they can demonstrate to the supervisory authority that all the following seven conditions are met:

1. LTEI holdings are well defined and managed separately from other activities
2. Commitment to hold LTEI holdings for a period that exceeds five years on average
3. Investments are European Economic Area (EEA) or Organisation for Economic Co-operation and Development (OECD) equities
   - Can be assessed at a fund level for European Social Entrepreneurship Funds, European Venture Capital Funds, European Long-Term Investment Funds, and closed-ended alternative investment funds with no leverage
   - These fund types can allow for non-EEA/OECD line items within
4. Insurer can avoid forced selling for at least five years into the future, even under stressed conditions
5. Insurer's risk management, asset-liability management (ALM) and investment policies are updated accordingly
6. LTEI holdings are diversified
7. LTEI holdings do not include participations

Quantitative Requirements

For the purposes of demonstrating their ability to avoid forced selling of equity investments on an ongoing basis and under stressed conditions, insurers can use either of the following two approaches:

1. ALM test (Article 171b)

   For life insurance liabilities, the insurer must demonstrate that the liabilities they want to apply LTEI to:

   a) have a Macaulay duration of more than 9.5 years

   b) mortality/lapse risk Solvency Capital Requirement (SCR) is less than 5% of Best Estimate Liabilities (BEL)

   c) such liabilities need to exceed LTEI holdings

   For non-life liabilities, the insurer would need to demonstrate that their liquidity buffer exceeds 100%, i.e. liquid assets, after haircuts, exceed the best estimate of non-life technical provisions net of reinsurance.

   Haircuts: Level 1 assets 0%; Level 2A 15%; Level 2B securitisations 25%; other Level 2B 50%; qualifying reinsurance/SPV flows 15% (50% otherwise).

2. Cash flow test (Article 171c)

   Insurers will be required to demonstrate that they are able to generate cash inflows that are higher than cash outflows over a five-year time horizon, both on an ongoing basis and under stressed conditions during each of the five-year testing periods. Stresses to increase the cash outflows for the insurer.

Investment Universe

Because all equity assets classified as LTEI attract the same 22% equity risk charge, the key driver of asset selection becomes the return-risk profile of each asset class.

As shown in the chart below (Figure 1), private market strategies offer the strongest return per unit of risk. Co-investment stands out with the highest return (16.04%) at a risk level (16.67%) similar to developed markets (DM) equity, giving a Sharpe ratio of 0.69. Private equity (11.85% return, 0.47 Sharpe) and capital solutions (10.37% return, 0.54 Sharpe) also compare well, with capital solutions delivering a comparable return to emerging market equity at roughly half the volatility (10.70% vs. 20.92%).

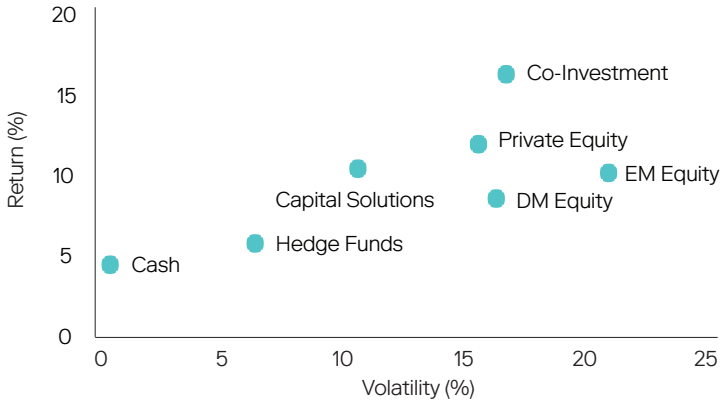
Public equity looks less compelling on a risk-adjusted basis. Developed market equity (8.56% return, 16.25% volatility, 0.25 Sharpe) and emerging markets (EM) equity (10.17% return, 20.92% volatility, 0.27 Sharpe) carry volatility at or above that of the private market strategies, with EM equity the most volatile asset in the set, yet both earn lower Sharpe ratios than every private market strategy shown.

Hedge Funds have the lowest risk of the equity-like assets (6.50%), but also the weakest Sharpe Ratio (0.19), as returns of 5.82% add little over cash (4.57%).

FIGURE 1

Private Market Strategies Offer the Strongest Risk-Adjusted Returns

Return, Volatility and Sharpe Ratio by Asset Class



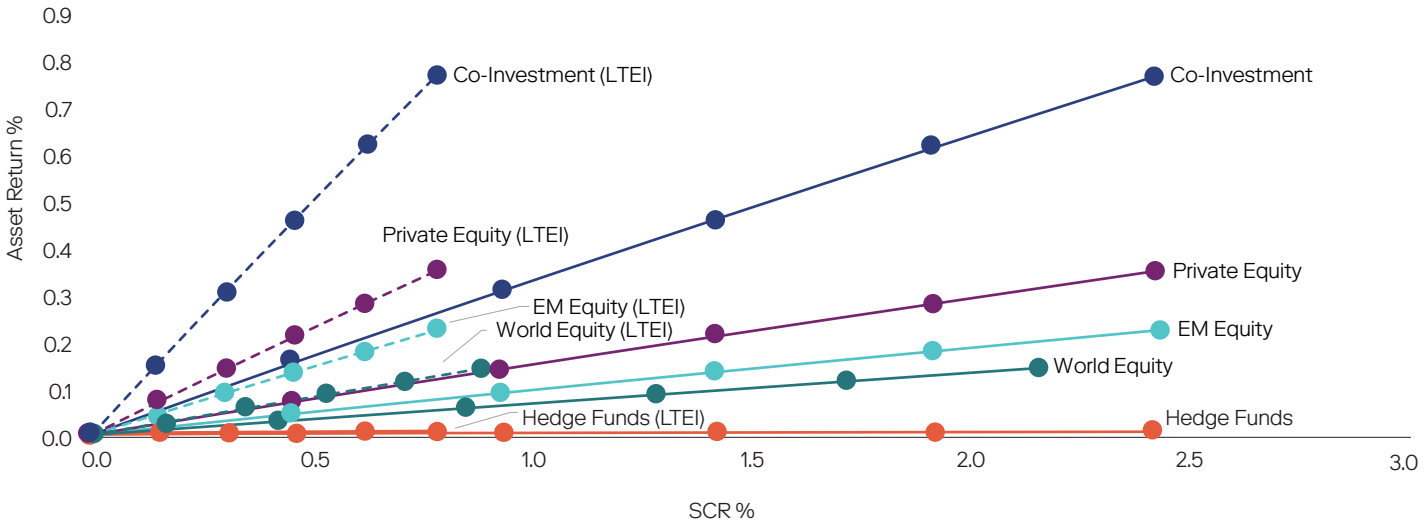
Asset Class	Return (%)	Volatility (%)	Sharpe ratio
Cash	4.57	0.63	
Capital Solutions	10.37	10.70	0.54
DM Equity	8.56	16.25	0.25
EM Equity	10.17	20.92	0.27
Hedge Funds	5.82	6.50	0.19
Private Equity	11.85	15.56	0.47
Co-Investment	16.04	16.67	0.69

Source: Neuberger, Bloomberg-Barclays, J.P. Morgan, Morningstar LSTA, FTSE Nareit, NCREIF, HFRI, Burgiss, infraMetrics; Analytics are as at 30 September 2026. **The performance and risk projections/ estimates are hypothetical in nature and reflect the Neuberger's Capital Market Assumptions as at 30 September 2026.** See the Indices Used and Index Definitions section at the end of this document for more information. The estimates do not reflect actual investment results and are not guarantees of future results. Actual returns and volatility may vary significantly. Asset classes are represented by benchmarks and do not represent any Neuberger investment product or service. Investing entails risks, including possible loss of principal.

FIGURE 2

Impact on Market SCR if Adopting LTEI

Return, SCR With and Without LTEI by Asset Class



Source: Neuberger, Bloomberg-Barclays, J.P. Morgan, Morningstar LSTA, FTSE Nareit, NCREIF, HFRI, Burgiss, infraMetrics; Analytics are as at 30 September 2026. **The performance and risk projections/ estimates are hypothetical in nature and reflect the Neuberger's Capital Market Assumptions as at 30 September 2026.** The estimates do not reflect actual investment results and are not guarantees of future results. Actual returns and volatility may vary significantly. Asset classes are represented by benchmarks and do not represent any Neuberger investment product or service. Investing entails risks, including possible loss of principal.

Key Considerations for Implementation

Liquidity: LTEIs require a commitment to hold for more than five years on average, so the illiquidity of private market strategies is less of a constraint than for other portfolios. The liquidity hurdle that typically deters insurers from investing in private equity therefore falls away once LTEI is adopted. Insurers that have favoured public equities mainly for their liquidity may wish to consider gaining more of their equity exposure through private markets, which, as shown above, offer better risk-adjusted returns under the same 22% capital charge.

Mark-to-market volatility: Reported volatility is typically lower in private markets, as holdings are valued periodically on an appraisal basis rather than marked to market daily. This smoothing helps stabilise own funds and the solvency ratio. It also means reported risk may understate the underlying economic risk, so insurers should not rely on the smoothed figures alone when assessing the true risk of these assets.

Macroeconomic environment: The return and risk figures above are five- to 10-year Capital Market Assumptions, and realised outcomes will depend on the economic backdrop. Higher interest rates raise the return hurdle from cash and can pressure valuations and exit conditions, while slower growth or weaker credit conditions may delay distributions and reduce returns on private equity and co-investments. Because the 22% charge is the same across all LTEI assets, insurers should assess the shortlisted asset classes against different rate, growth and inflation scenarios, and diversify by vintage year, geography and strategy rather than concentrate in the highest-returning asset class.

Next Steps

With the new rules applying from the end of January 2027, insurers that want to use LTEI treatment from day one should act now: identify desired equity holdings that qualify as LTEI, choose between the ALM and cash flow tests, update their risk management, ALM and investment policies, and engage early with their supervisor.

In parallel, investment teams should revisit their strategic asset allocation to reflect post-reform asset class attractiveness. With a single 22% capital charge, return per unit of risk, rather than capital cost, becomes the main driver of choice between equity asset classes, and private market equity strategies could be considerably more attractive than before.

Disclaimers

Asset Class Assumptions & Estimates

Capital market assumptions used herein reflect Neuberger's forward-looking estimates of the benchmark return or volatility associated with an asset class (see the Indices Used and Index Definitions section below) Estimated returns and volatilities are hypothetical return and risk estimates generated by Neuberger's Institutional Solutions Group. Estimated returns and volatilities do not reflect the alpha of any investment manager or investment strategy/vehicle within an asset class. Information is not intended to be representative of any investment product or strategy and does not reflect the fees and expenses associated with managing a portfolio or any other related charges, such as commissions and surrender charges. Estimated returns and volatilities are hypothetical and generated by Neuberger based on various assumptions and inputs, including current market conditions, historical market conditions and subjective views and estimates. Capital market assumptions shown reflect Neuberger's long-term (20+ years into the future) estimates or intermediate-term (five to 10 years into the future) estimates which are reviewed at least annually. Results will differ depending on whether they are based on Neuberger's long-term (20+ years into the future) or intermediate-term (five to 10 years into the future) capital market assumptions. Neuberger's capital market assumptions are derived using a building block approach that reflects historical, current, and projected market environments, forward-looking trends of return drivers, and the historical relationships asset classes have to one another. These hypothetical returns are used for discussion purposes only and are not intended to represent, and should not be construed to represent, predictions of future rates of return. Actual returns may vary significantly. Neuberger makes no representations regarding the reasonableness or completeness of any such assumptions and inputs. Assumptions, inputs, and estimates are periodically revised and subject to change without notice. Estimated returns and volatilities should not be used, or relied upon, to make investment decisions.

Rate of Return Estimate: Rate of return or geometric return is a measure of average returns of an investment over a period of time. Geometric rates of return are typically referred to as annualised compound rates of return and are always less than or equal to the arithmetic mean return of the same time series. Geometric rates of return are used for straight line calculations within the analysis, for example, the cash flow calculations. In straight-line calculations, each year is represented as a gain, so the compound (geometric mean) rate of return is used to adjust for the amount needed to make up for a loss in a given year. For example, if you lose 5% in one year, and gain 5% the year after, you still have less than you started with at the beginning of year one.

Arithmetic Mean Estimate: Arithmetic mean or average return is calculated by dividing the sum of a series of numbers by the number of overall items. This is more typically thought of as an "average" of the data set. Arithmetic mean or average return ignores the impact of compounding in the context of analysing investment returns and is the simple average of returns observed over a period of time. Arithmetic mean returns are used in this material and, if applicable, the Efficient Frontier, because, through randomisation, losses and gains are being accounted for each year.

Standard Deviation: A statistical measure of the volatility based on the distribution of a set of data from its mean (average value). For example, a portfolio with an average return of 10% and a standard deviation of 15% would return a result between -5% and +25% the majority of the time (68% probability or 1 standard deviation), almost all of the time the return would be between -20% and +40% (95% probability or 2 standard deviations). For a 0 standard deviation, the result would always be 10%. Generally, more aggressive portfolios have a higher standard deviation and more conservative portfolios have a lower standard deviation.

Indices Used and Index Definitions

Asset Class	Benchmark Index	Index Definition
Cash	Bloomberg US Treasury Bill Index	The **Bloomberg US Treasury Bill Index** tracks the performance of the US Treasury bill market for public obligations issued by the US government.
Capital Solutions	ICE BofA 8% Constrained Core West Preferred & Jr Subordinated Securities Index ICE BofA US Convertibles Index S&P 500	The **ICE BofA 8% Constrained Core West Preferred & Jr Subordinated Securities Index** is a custom fixed-income benchmark that tracks the performance of US dollar-denominated preferred stock and junior subordinated corporate debt issued by companies in the United States and Western developed markets. The **ICE BofA US Convertibles Index** is a market-capitalization-weighted, rules-based benchmark that tracks the performance of publicly issued US domestic corporate convertible securities. The **S&P 500 Index** is a stock market index that tracks the performance of 500 large publicly traded companies listed on stock exchanges in the United States.
DM Equity	MSCI World	The **MSCI World Index** is a global stock market index that tracks large- and mid-cap companies across developed countries.
EM Equity	MSCI Emerging Markets Index	The **MSCI Emerging Markets Index** is a market-value weighted index designed to represent the performance of large- and mid-cap securities in 26 emerging markets.
Hedge Funds	Hedge Fund Research Index	The **HFRI (Hedge Fund Research Index)** is a widely recognised family of benchmark indices that tracks the performance of the global hedge fund industry.
Private Equity	Burgiss	The **MSCI Burgiss Private Capital Indexes** are a set of transparent, cash-flow-based benchmarks that measure the aggregate performance, cash flows, and net asset values (NAVs) of private capital funds.
Co-Investment	Burgiss	The **MSCI Burgiss Private Capital Indexes** are a set of transparent, cash-flow-based benchmarks that measure the aggregate performance, cash flows, and net asset values (NAVs) of private capital funds.

Past performance is no guarantee of future results.

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