American Property Casualty Insurance Association

INSURING AMERICA apci.org

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March 18, 2021

The Honorable Pat Toomey
Ranking Member
Committee on Banking, Housing, and Urban Affairs
United States Senate
Washington D.C., 20510

Re: Request for Proposals for Improving the Market for Private Capital

Dear Senator Toomey:

The property/casualty insurance industry shares your view that improving the market for private capital will lead to better investment opportunities, not only for retail investors, but also for insurers. As you know, insurers are large scale investors in governmental securities, specifically in the U.S. treasury securities and the municipal bond markets. Municipal bonds typically have been the preferred vehicle for attracting investment in local infrastructure projects.

If properly structured, we believe other vehicles for investing in infrastructure projects also could prove to be viable opportunities for attracting private capital from insurers and retail investors. The country needs to upgrade deteriorating roads, repair aging bridges, and fortify susceptible water treatment facilities. The capital markets can help address these needs.

One of APCIA's priorities is to encourage mitigation and resilience projects and efforts, which can include public infrastructure projects. Resilient focused projects likewise could attract capital for developing sustainable, environmentally friendly facilities that not only enhance the quality of life for local communities, but also provide satisfactory investment returns.

In order to take full advantage of infrastructure opportunities, significant obstacles must be addressed. We have identified key challenges that deserve further study in order for the property/casualty insurance industry to pursue additional infrastructure development.

1) The term "infrastructure" is a broad concept, but there is no universally accepted definition.
   a) A more precise definition of infrastructure is needed to facilitate a consistent approach for evaluating infrastructure investment risks.

2) Property/Casualty insurance companies are large scale investors in the municipal bond market.
   a) Although municipal bonds are long-term, they trade in deeply liquid markets.
   b) That liquidity is an important requirement for property/casualty insurers because sudden, exigent circumstances, i.e., catastrophes, may require liquidation of muni investments.

c) Investment in infrastructure projects must be structured in a manner that provides ongoing liquidity.

3) Eligible infrastructure projects must produce an income stream, such as user fees or availability payments.
   a) Income streams will be necessary to pay off the debt and provide acceptable returns for investors.
   b) The paucity of qualifying infrastructure projects will limit pool of investors, including property/casualty insurers.

4) To invest in infrastructure projects, property/casualty insurers and other investors require information about the infrastructure risks.
   a) Risk information is traditionally provided through debt ratings; however, infrastructure debt instruments typically are unrated due to their relatively smaller size or because they are privately placed.
   b) Unrated investments must undergo onerous and expensive rating process by the National Association of Insurance Commissioners (NAIC) in order to be recognized as capital.
   c) Lack of public rating may adversely impact market value of the infrastructure debt.
   d) Better market information is necessary for evaluating infrastructure risks.

5) Infrastructure projects relate to facilities with long usable lifespans.
   a) Fluctuating interest rates impact the valuation of the debt securities that fund infrastructure projects, and that valuation becomes increasingly difficult for long-lived assets.
   b) The inability to price interest rate risk beyond a 10-year window limits the population of investors willing and able to invest in infrastructure projects.
   c) The interest rate volatility over the long useful life of the infrastructure project increases the difficult for pricing and placing infrastructure debt.
   d) Potential investors in resilient infrastructure projects need a transparent pricing mechanism that provides confidence that the net present value interest stream is reliable.

6) Although infrastructure investments are generally considered stable, there are risks over their life cycle.
   a) There are early-stage risks, such as bureaucratic and permitting delays.
   b) During the construction period, there will be physical damage and liability concerns.
   c) Upon commencement of operations, there will be ongoing physical and liability risks.
   d) Property/casualty insurers generally can provide insurance products to protect against the various property and liability risks through all phases of the infrastructure project.

Private investment in infrastructure will help produce economic growth, while reducing future costs. APCIA is interested in finding ways to encourage private investment in public infrastructure projects. Doing so, however, requires solutions to several challenges, summarized below:

- Defining the concept of infrastructure;
- Developing infrastructure investment vehicles that provide liquidity;
- Identifying eligible infrastructure projects;
- Providing better market information for evaluating infrastructure investment opportunities;
- Developing a transparent pricing mechanism that provides a reliable net present value interest stream; and
- Developing approaches for identifying and addressing the infrastructure risks that arise throughout the life cycle of the project.

These issues require more study in order to develop a clear strategy for resolving these concerns. APCIA welcomes the opportunity to work with you and your staff toward these solutions.

Sincerely,

Nathaniel F. Wienecke