

TAILORING INSURANCE INVESTMENTS

YIELD ENHANCEMENT STRATEGIES TO OPTIMIZE CAPITAL-CONSTRAINED INSURANCE PORTFOLIOS

In today's complex investment landscape, insurance investors are required to balance multiple, often competing objectives. As they navigate an environment of heightened market volatility and evolving regulatory pressures, three key questions emerge:

1. How can insurers optimize their yield profile without compromising risk management priorities?
2. What strategies offer the most efficient use of increasingly scarce regulatory capital?
3. Perhaps most important, where can investors uncover structural alpha that persists across market cycles?

Three key strategies emerge as potential answers to these questions—**Private Asset-Based Finance (Private ABF)**, **Transitional Commercial Mortgage Loans (Transi CMLs)**, and **Direct Lending (DL)** through rated feeder structures. We believe these strategies may have the potential to provide compelling solutions for insurance investors seeking to enhance portfolio yield.

1. ENHANCED YIELD VIA ILLIQUIDITY PREMIUM: PRIVATE ASSET-BASED FINANCE

Asset-Based Finance represents a potential opportunity for insurers with sufficient liquidity to seek enhanced yields while managing portfolio credit rating impact. This strategy has historically exhibited risk-adjusted returns that compare favorably to traditional corporate debt instruments.

Key Advantages

Recently, [Private ABF](#) has typically delivered spreads in excess of 150 basis points above comparably rated public corporate bonds, representing significant income generation potential and attractive absolute return opportunities.¹ Private ABF investments also benefit from comprehensive structural protections and robust collateralization mechanisms that enhance credit quality. Further, the strategy's underlying asset exposure and

variety of collateral types offer material diversification benefits as compared to traditional corporate debt. While differentiated sources of capital and greater surety of execution are common reasons why borrowers seek non-bank lending, the breadth and depth of origination capabilities underscore an asset manager's capabilities in this asset class.

Portfolio Insights

Due to the relative illiquidity of Private ABF, investments require consideration around portfolio construction and asset-liability matching with a longer-term investment approach. Investors should maintain adequate liquidity buffers to account for potential stress scenarios. However, for insurers with long-dated liabilities and strong liquidity positions, the illiquidity premium represents an attractive source of incremental yield.

¹ Source: PGIM (Public & Private Fixed Income Group) Spread over comparably rate public corporate bonds is based on a 10-year time horizon. BBG Corporate spreads as of August 31, 2025.

2. CAPITAL-EFFICIENT YIELD ENHANCEMENT: TRANSITIONAL COMMERCIAL MORTGAGE LOANS

Transitional CMLs can present a distinctively attractive opportunity from both a yield and capital efficiency perspective, especially for insurers operating under US and Bermuda regulatory frameworks. These are typically internally rated BB+ and designated either CM2 or CM3 loans based on NAIC standards.

Key Advantages

The current market provides yields of SOFR plus 280-400 basis points, delivering compelling return potential. Under the Bermuda regulatory framework, these investments are typically assigned a capital factor of 5%, representing highly efficient capital deployment. In comparison, traditional BB rated corporate bonds offer lower yields while consuming 8% of capital.² This dynamic ultimately creates differentiated capital efficient yield enhancement opportunities. While the figures are different in the US, the relative attractiveness still applies. The floating rate nature of Transitional CMLs provides natural protection against interest rate risk, while direct origination allows for customized structural protections and covenants.

Portfolio Insights

Transitional CMLs require deep real estate expertise and market knowledge, with manager sourcing capabilities being particularly important given the private nature of the asset class. Unlike traditional securitized products that rely on standardized borrower profiles, Transitional CMLs require highly specialized borrower relationships and bespoke deal structures, supported by robust origination networks and deep direct lending expertise.

The transitional nature of the underlying assets poses risks related to property improvements or repositioning. A detailed understanding of local market dynamics and property-specific factors should be top-of-mind for investors. Additionally, Transitional CMLs offer attractive portfolio diversification benefits, exhibiting low correlation to traditional asset classes due to their differentiated risk-return profile and sensitivity to real estate fundamentals. Regulatory requirements may vary by jurisdiction so careful analysis of capital treatment should also be a priority.

3. RBC EFFICIENCY: DIRECT LENDING RATED FEEDER STRUCTURES

The implementation of direct lending strategies through rated feeder structures represents a capital efficient opportunity to capture attractive yields.

Key Advantages

Direct lending instruments provide yields of approximately SOFR plus 550 basis points, offering favorable spread relative to comparably rated public bonds.³ The rated feeder structure offers meaningful regulatory capital benefits for US- and Bermuda-domiciled insurers by consuming meaningfully less NAIC RBC or BSCR compared to investing in the underlying whole loans directly on balance sheet. This results in higher yield per unit of capital.

Portfolio Insights

Rated feeders benefit from the robust diligence of the selected NRSRO. Regulatory engagement across multiple jurisdictions may also be required to unlock capital efficiency benefits. The rated feeder structure also requires liquidity management related to capital calls. Ongoing monitoring will be key in addressing underlying loan performance and structuring.

Increasingly, rated feeder structures can be tailored to provide bespoke solutions and deployed across both separately managed accounts (SMAs) and pooled fund formats (commingled vehicles) providing flexibility to meet investor needs. Additionally, rated feeder structures can be developed to facilitate horizontal tranche transfers and secondary market transactions, providing liquidity to insurance investors in the direct lending rated-feeder space.

² Source: PGIM (Real Estate Group). Production and spread is based on an 8-year time horizon. Data as of as of August 31, 2025. Includes senior floating loans only.

³ Source: PGIM Private Credit. Data as of as of August 31, 2025. Spreads are based on deployment and pipeline statistics. Bond index references: ICE BofA US HY Index.

STRATEGIC PORTFOLIO IMPLEMENTATION

Successful implementation of these strategies requires a holistic approach to portfolio construction. Investors may want to further explore three key areas from this perspective:

1. Capital Budget Allocation

Optimal regulatory capital consumption requires sophisticated modeling and ongoing monitoring processes. Risk-adjusted return metrics must incorporate both explicit and implicit capital costs across the portfolio. Jurisdictional variations in treatment demand careful consideration in portfolio construction decisions.

2. Liquidity Management

Regular portfolio-level liquidity stress testing ensures resilience under adverse scenarios. Comprehensive cash flow matching analysis supports optimal asset-liability management. Detailed contingency funding planning provides protection against market disruptions.

3. Risk Management

Robust credit monitoring capabilities ensure early identification of potential issues. Thoughtful sector and geographic diversification mitigate concentration risk. Correlation analysis with existing portfolio exposures supports optimal portfolio construction.

INVESTMENT IMPLICATIONS

For insurance investors, the implications are clear: deploying new and diverse strategies across private assets may provide additional opportunities to enhance yield.

Public market bonds are necessary but insufficient in capital constrained portfolios with yield targets. The spread premium available in private markets, particularly through Private ABF,

Transitional CMLs, and DL, may offer incremental return potential that is difficult to replicate in public markets.

Next, regulatory capital efficiency has become a key differentiator. The ability to implement strategies that seek enhanced yields while consuming less capital can improve overall portfolio efficiency. This is not just about reducing capital charges—it is also about fundamentally improving the relationship between risk, return, and regulatory capital consumption.

Finally, the opportunity set in private credit markets has expanded significantly, along with its complexity. Success for investors in the space will require both access to these strategies and a partner who has the appropriate frameworks, tools, as well as expertise to evaluate, implement, and monitor each strategy effectively. One valuable differentiator among market participants is the ability to directly originate private assets rather than rely exclusively upon sponsors and banks.

LOOKING AHEAD

Going forward, insurance investors who can successfully integrate these strategies while navigating their complexities will likely emerge as market leaders. The key to success lies not just in understanding these opportunities but in executing them within a cohesive portfolio framework that aligns with an insurer's specific liability profile and regulatory constraints.

With current spreads and regulatory frameworks continuing to evolve, insurers who choose to implement these strategies may capture significant advantages. Those who wait may find themselves playing catch-up in an increasingly competitive landscape.

One potential path to enhanced portfolio efficiency runs through private markets, and the tools for optimizing this opportunity set are available. The question is no longer whether to implement these strategies, but how to do so most effectively to favorably differentiate the insurance investor.

The landscape for insurance investors has fundamentally shifted. The convergence of regulatory requirements, market complexity, and the persistent search for yield has created both challenges and opportunities. Private ABF, Transitional CMLs, and DL all offer compelling opportunities for insurers to enhance portfolio yield while optimizing capital efficiency. However, these three strategies represent more than simple portfolio adjustments—they illustrate strategic reimagining of how insurance portfolios can be constructed to achieve multiple, often competing objectives.

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ADDITIONAL CITATIONS

1. Source of calculations: PGIM (Public & Private Fixed Income Group). Acquisition spread premium represents the difference in yield at the time of purchase between a private ABF investment and a comparable public corporate bond. This premium reflects the additional yield typically associated with the complexity, illiquidity, and structuring characteristics of private debt markets. The spread premium is calculated by matching rating and WAL to the following indices: Bloomberg US Corporate 1-3 Yr Total Return Index Value Unhedged (LF99TRUU), Bloomberg US Corporate 3-5 years Total Return Index Value Unhedged (BUS3TRUU), Bloomberg US Corporate 5-7 years Total Return Index Unhedged (I13282US), Bloomberg US Corporate 7-10 years Total Return Index Unhedged (I13283US), Bloomberg US Corporate 10+ years Total Return Index Unhedged (I13284US), Bloomberg Intermediate US High Yield Total Return Index Unhedged (I00166US), Bloomberg Long U.S. High Yield Total Return Index Unhedged (I00319US).
2. Production and spread is based on an 8-year time horizon. Data as of August 31, 2025. Spreads are for the senior loan only but don't count in ancillary income received under the loan, including origination and extension fees in additional annual spread during the term.
3. The benchmark of SOFR + 550bps for direct lending is supported by PGIM's historical and pipeline Direct Lending deal data, which is based on weighted spreads across closed and pipeline transactions.

For comparison to similarly rated public bonds, the reference index is the ICE BofA US High Yield Single-B Index, which provides a consistent measure of public market spreads. The timeframe for this analysis includes both historical transactions and current pipeline deals in PSLO II, our 2023 vintage Direct Lending Fund.

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