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INSURANCE SOLUTIONS

Four Themes Emerging in Life Insurers' Asset Allocations

INSIGHTS

Life insurers are continuing to move toward less liquid securities—which provide the potential for yield enhancement—while simultaneously de-risking from a credit perspective.

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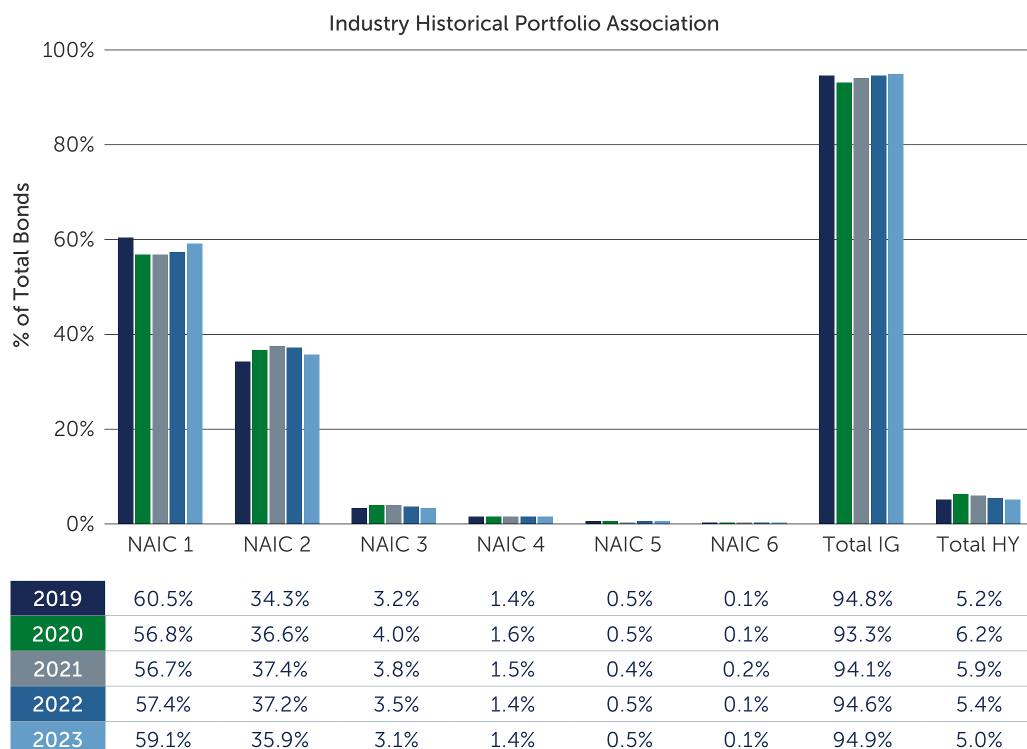
Insurance companies have recently released their statutory filings for year-end 2023, presenting an opportunity for a deep dive into what's driving asset allocations within life insurers' portfolios. While some new trends have emerged, there are also old trends that have continued and some that have been broken from this year's data. Below we highlight four key themes that are shaping asset allocations for life insurers.

"Overall, life insurers are seeking capital efficiency by allocating toward higher-rated securities unless spread levels compensate for higher capital and risk."

1. Up in Credit Quality

Allocations to the highest rated NAIC 1 class (A- and higher) have continued higher since 2022 when the industry broke a string of five years of declining allocations. In particular, allocations increased by 1.7% from the year prior, to 59.1% of total bonds **(Figure 1)**. Within NAIC 1, AAA-rated growth has been flat with increases seen mainly in the AA and A-rated categories. This credit improving increase in NAIC 1 has largely come from the NAIC 2 (BBB+/-) class, which saw a stark reduction of 1.3% of total bonds from 2022. High yield allocations have also been declining since hitting a peak in 2020.

Figure 1: Moving Up in Quality



	NAIC 1	NAIC 2	NAIC 3	NAIC 4	NAIC 5	NAIC 6	Total IG	Total HY
2019	60.5%	34.3%	3.2%	1.4%	0.5%	0.1%	94.8%	5.2%
2020	56.8%	36.6%	4.0%	1.6%	0.5%	0.1%	93.3%	6.2%
2021	56.7%	37.4%	3.8%	1.5%	0.4%	0.2%	94.1%	5.9%
2022	57.4%	37.2%	3.5%	1.4%	0.5%	0.1%	94.6%	5.4%
2023	59.1%	35.9%	3.1%	1.4%	0.5%	0.1%	94.9%	5.0%

Sources: S&P Global. As of December 31, 2023.

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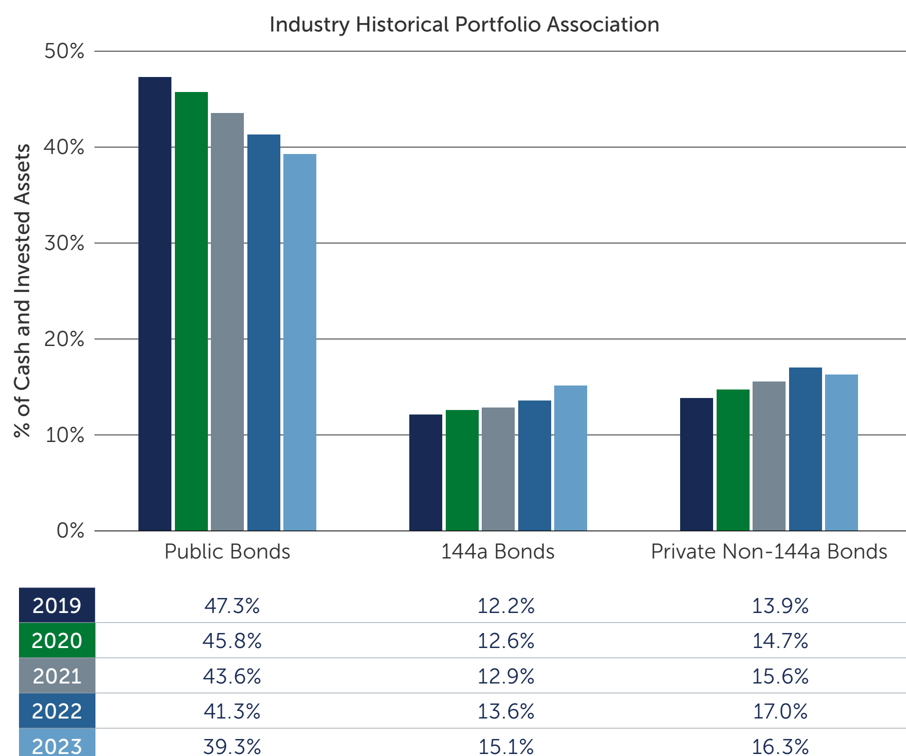
2. Private Bond Allocations Rise

Allocations to public bonds have continued their long trending descent by dropping 2.0% year-over-year **(Figure 2)**. While still the predominant asset class for life insurers, their allocations have fallen by 8.0% over the past five years to 39.3%. Meanwhile, 144a private bonds continued their trend higher, increasing 1.5% year-over-year to 15.1%. However, non-144a privates—also known as true privates—fell for the first time in five years, slipping 0.7% over the past year.

Figure 2: Increasing Allocations to 144a Private Bonds



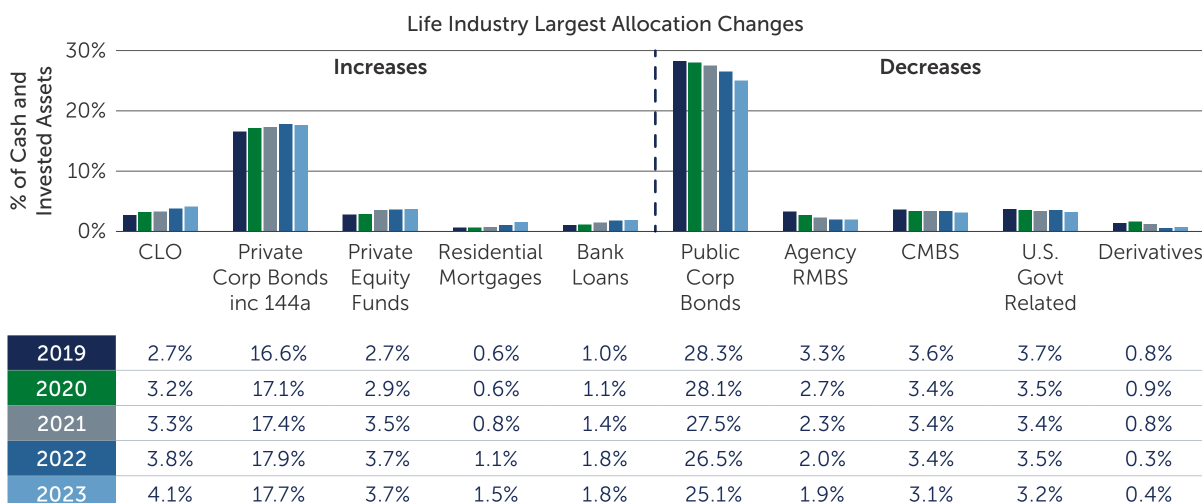
	Public Bonds	144a Bonds	Private Non-144a Bonds
2019	47.3%	12.2%	13.9%
2020	45.8%	12.6%	14.7%
2021	43.6%	12.9%	15.6%
2022	41.3%	13.6%	17.0%
2023	39.3%	15.1%	16.3%

Sources: S&P Global. As of December 31, 2023.

3. Shift Toward Select Structured Assets

Given the attractive current yields on offer and capital efficiency, residential mortgages—also known as non-securitized whole loan mortgages—logged the biggest yearly gain of all asset classes **(Figure 3)**. Though a seemingly small 0.4% overall allocation increase, it represents a 42% increase within the class. Certain structured asset classes also saw an increase in allocation led by collateralized loan obligations (CLOs), asset-backed securities, and non-agency residential mortgage-backed securities. Meanwhile, concerns about the commercial real estate market softened the allocation to commercial mortgage-backed securities.

Figure 3: CLOs Continue to be the Fastest Growing Asset Class



	CLO	Private Corp Bonds inc 144a	Private Equity Funds	Residential Mortgages	Bank Loans	Public Corp Bonds	Agency RMBS	CMBS	U.S. Govt Related	Derivatives
2019	2.7%	16.6%	2.7%	0.6%	1.0%	28.3%	3.3%	3.6%	3.7%	0.8%
2020	3.2%	17.1%	2.9%	0.6%	1.1%	28.1%	2.7%	3.4%	3.5%	0.9%
2021	3.3%	17.4%	3.5%	0.8%	1.4%	27.5%	2.3%	3.4%	3.4%	0.8%
2022	3.8%	17.9%	3.7%	1.1%	1.8%	26.5%	2.0%	3.4%	3.5%	0.3%
2023	4.1%	17.7%	3.7%	1.5%	1.8%	25.1%	1.9%	3.1%	3.2%	0.4%

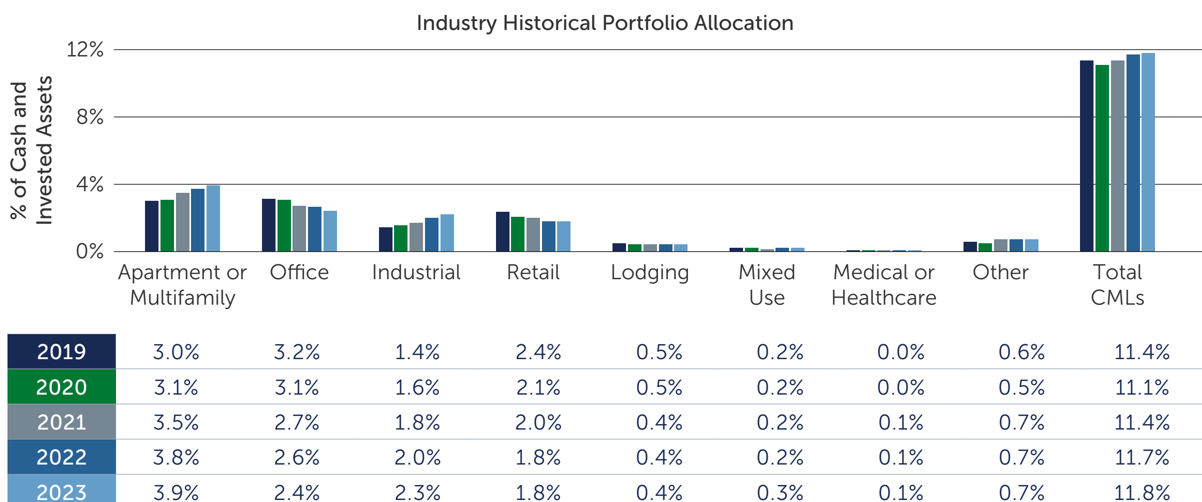
Sources: S&P Global. As of December 31, 2023.

CLOs continued their march higher as the fastest growing asset class over the past five years with an allocation of 4.1%, up from 3.8% last year. Bank loans, which includes portfolio finance (NAV lending), held steady year-over-year after strong growth in the last few years. Public corporate bonds fell by 1.4%, which was by far the biggest reduction of any class.

4. Increase in Lower-rated Commercial Mortgages

Commercial mortgage allocations had a slight uptick year-over-year. Within commercial mortgages, the life industry continued to rapidly reduce exposure to the office sector given concerns about vacancy rates post-COVID **(Figure 4)**. Retail also showed slight declines in allocation. Meanwhile, apartment, multi-family, and industrials showed significant increases, continuing a five-year rebalancing trend within the asset class.

Figure 4: Exposure to Office Sector Continues to Decline

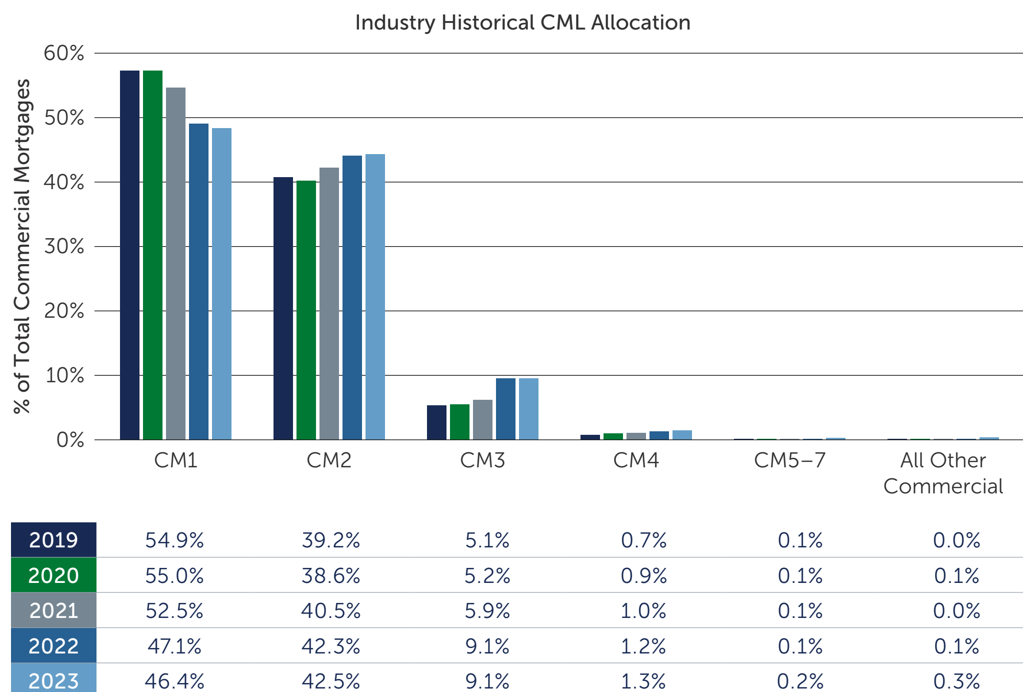


	Apartment or Multifamily	Office	Industrial	Retail	Lodging	Mixed Use	Medical or Healthcare	Other	Total CMLs
2019	3.0%	3.2%	1.4%	2.4%	0.5%	0.2%	0.0%	0.6%	11.4%
2020	3.1%	3.1%	1.6%	2.1%	0.5%	0.2%	0.0%	0.5%	11.1%
2021	3.5%	2.7%	1.8%	2.0%	0.4%	0.2%	0.1%	0.7%	11.4%
2022	3.8%	2.6%	2.0%	1.8%	0.4%	0.2%	0.1%	0.7%	11.7%
2023	3.9%	2.4%	2.3%	1.8%	0.4%	0.3%	0.1%	0.7%	11.8%

Sources: S&P Global. As of December 31, 2023.

From a credit perspective, commercial mortgages saw a slight decrease in the highest-rated category, CM1 **(Figure 5)**. At the same time, allocations increased in the lower-rated CM 2-5 categories supported by the attractive current yields on offer, continuing a trend from the last few years.

Figure 5: Allocations Shift to Lower-rated CM 2-5



	CM1	CM2	CM3	CM4	CM5–7	All Other Commercial
2019	54.9%	39.2%	5.1%	0.7%	0.1%	0.0%
2020	55.0%	38.6%	5.2%	0.9%	0.1%	0.1%
2021	52.5%	40.5%	5.9%	1.0%	0.1%	0.0%
2022	47.1%	42.3%	9.1%	1.2%	0.1%	0.1%
2023	46.4%	42.5%	9.1%	1.3%	0.2%	0.3%

Sources: S&P Global. As of December 31, 2023.

Key Takeaway

Overall, life insurers are seeking capital efficiency by allocating toward higher-rated securities unless spread levels compensate for higher capital. 2023 saw continued movement toward less liquid securities which provide compensation for insurers that can afford the illiquidity risk, allowing for potential yield enhancement while simultaneously de-risking from a credit perspective.

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