

Sub IG Infra Debt: Exploring the Risk Spectrum for Insurers

INSIGHTS

Infrastructure debt has moved beyond toll roads to sectors like data centers and battery storage. For insurers, sub-IG infra debt can offer stability, yield and capital efficiency and can help achieve both financial and strategic objectives in today's market.



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Once dominated by monolithic assets like toll roads and power plants, the infrastructure market now spans everything from data centers to battery storage—driven by digital transformation, sustainability imperatives and global funding gaps. With governments facing budget and fiscal challenges, and banks unable to meet surging capital demand alone, private lenders are stepping in and reshaping how critical infrastructure is financed. **For insurers, selective exposure to sub-investment grade (sub-IG) infra debt can help achieve both financial and strategic objectives in today's market.**

Infrastructure debt is not new to insurance investors. Many insurers have been investing for years, attracted to infrastructure debt's **asset-backed security, predictable cash flows and portfolio diversification**. In many capital regimes, the asset class also benefits from preferential capital treatment versus corporate lending (qualifying criteria apply), enhancing returns on regulatory capital.

Historically, much of the focus for insurers has been on investment grade (IG) infrastructure debt to match long-term liabilities. However, there is growing recognition that **select sub-IG opportunities can offer compelling risk-adjusted returns**. With spreads remaining tight across public markets and, to a lesser extent, certain private markets, insurers are increasingly seeking ways to enhance portfolio yields without significant compromise on credit discipline. Sub-IG infrastructure debt stands out, offering yields that are comparable to core infrastructure equity, while still providing the downside protection inherent in real asset-backed debt.

Assessing Opportunities in Sub-Investment Grade Infrastructure Debt

When moving up the risk curve, maintaining discipline in underwriting standards becomes even more critical. While higher returns often come with greater credit risk, it's important to recognize that not all credit risks are created equal. In fact, the transactions we originate for clients in this space tend to fall into two distinct categories:

1. FINANCIAL RISK

We selectively pursue deals with elevated financial risk, such as structurally or contractually subordinated positions, only when the underlying businesses are large, typically investment grade, and supported by predictable cash flows and substantial equity cushions. These characteristics help justify the potential for higher returns. In addition, we require these businesses to demonstrate **high barriers to entry**, have a **strong asset base**, operate in **markets with strong fundamentals** and demonstrate a **consistent track record of stable dividend distributions**.

Our preference is to work with **well-capitalized, experienced global equity sponsors** seeking to further lever their operational infrastructure platform businesses, often for the purpose of growing the underlying asset base. Sponsors may choose to issue subordinated debt instead of incremental senior debt to ensure the underlying asset maintains strong investment grade credit metrics.

For instance, we recently invested in a subordinated position in a European rolling stock lessor, internally rated as a strong sub-investment grade under our own internal ratings methodology. The operating business is investment grade rated and benefits from **stable long-term cashflows, strong asset backing and a significant equity cushion**. Our investment offered strong relative value compared to equivalent public BB credits.

2. BUSINESS RISK

An alternative strategy for achieving higher returns involves investing on a **senior-secured basis while taking on additional business risk**. These transactions often benefit from their senior-secured status, with **first priority claims on the cash flows and assets**. Any residual amounts beyond these claims are available to the subordinated creditors and equity investors.

Businesses that fit this return profile are typically greenfield in nature, face greater competitive pressures and have less contracted or more variable cash flows, as well as other operational uncertainties. Asset selection is therefore critical. We aim to avoid investments in **new or unproven technologies**, transactions involving overly complex construction, or those **reliant on sustained or rising commodity prices** to support debt repayment.

A recent example is our senior-secured investment in a North American business-to-business fiber company. As a “brownfield” opportunity with a proven operating history, the asset was already generating **substantial cash flow, which was more than sufficient to cover debt service**. This was a key differentiator in a sector often dominated by greenfield investments with **high capital expenditure requirements and uncertain paths to profitability**. Overall, we viewed the opportunity favorably, with the increased returns appropriately compensating for the additional business risk stemming from shorter-term contracts and the company’s competitive positioning.

We avoid combining **high business risk with subordinated positions**, as this can significantly increase the risk profile of a given transaction, typically resulting in a single-B credit. Our strategy focuses on **high-quality, cash-generating, defensive BB credit quality assets**.

Private Infrastructure Debt: A Compelling Risk-Return Profile

Private infrastructure debt investments are often unrated unless a rating is specifically required typically for regulatory reasons, such as insurance mandates in jurisdictions like the U.S. and Bermuda. Our internal credit assessments generally map these assets to a **BB or BB+ rating**. Yields on these investments often **approach those of core infrastructure equity**, while offering the added protections of secured debt and substantial equity buffers. This combination creates an attractive risk-return profile for investors seeking higher income with meaningful downside protection.

The sub-IG infrastructure debt market is significantly smaller than its investment grade counterpart, making strong origination capabilities and deep sector expertise essential. **Passive allocation is not an option in private markets**. Manager dispersion is pronounced, and default experience can vary widely across managers, sectors and geographies. Success in this segment ultimately hinges on the ability to identify resilient assets, structure transactions prudently and actively manage risk throughout the investment lifecycle.

One of the key advantages of lending in private markets is the flexibility to negotiate **bespoke deal terms** and tailor covenants to address **transaction-specific risks**—a feature that is particularly valuable in sub-IG investments. To fully capitalize on this advantage, insurers benefit from partnering with managers who have **both capital to deploy and deep market experience**, enabling them to shape deal terms and manage risk effectively.

Infrastructure CLOs

Beyond direct and fund allocations, **infrastructure collateralized loan obligations (CLOs)** are a nascent but growing way for investors to access sub-IG infrastructure debt. **CLOs offer a scalable and often familiar structure for insurers to invest in infrastructure debt**, which can otherwise be illiquid and difficult to source directly.

The tranching mechanism also provides flexibility for tailoring exposure:

- Risk-averse insurers can take advantage of the **cashflow waterfall mechanisms** within a CLO structure to **protect their capital**.
- Yield-seeking insurers can further lever returns through mezzanine and equity tranches, including delivering returns within policyholder books.

This ability to structure **sub-IG infrastructure debt into IG and HY exposures** allows insurers under many regimes across North America and APAC, and to a lesser extent in Europe,¹ to uplift their **reserve, surplus and/or policyholder portfolios in a tailored and capital-efficient way**.

Conclusion

Insurers today face a challenging environment: **yields on traditional assets remain compressed**, while regulatory and liability pressures persist. Infrastructure debt, particularly sub-IG segments, now offer a practical route to **higher income without abandoning prudent risk management**.

Sub-IG infra debt can provide access to **enhanced returns supported by real assets and tailored structures** at a time when public markets offer limited compensation for risk. For insurers seeking portfolio diversification and improved capital efficiency, allocating to this space is not just timely; **it is increasingly necessary as private capital becomes central to funding essential infrastructure**.

1. Applies to Solvency II internal model firms, as well as to a lesser extent in Switzerland, and following expected Solvency II reforms in the EEA.

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