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Markets Insights

The real risk of private credit's involvement in the pension business

The critical issue is liquidity and ensuring that long-term promises to pay retirement benefits are met

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In the last decade, there has been a sharp turn in the market share of the US annuity business as a result of some big structural shifts.

The fastest-growing issuers of annuities now are a bunch of asset managers who have built their own insurance companies or acquired one to add to their stable of financial services. The pace of that takeover should worry anyone who owns one of these products.

A Federal Reserve Bank of Chicago working paper from 2025 found that private-equity-owned life insurers increased their market share of annuities sold in the US from 8.5 per cent to 18 per cent between 2017 and 2024. Some 61 per cent of this growth can be attributed to private credit investments. Legacy insurers have historically not had "in-house" access to such products, making it difficult for them to compete against private capital-owned insurers.

And what is also new in this private credit involvement are the destinations of the capital. Much of it is supporting the huge investment in AI infrastructure such as data centres and chips. And some of this, as the Bank for International Settlements has recently highlighted, has been through off-balance-sheet borrowing by the AI hyperscalers. This poses unknown risks for insurers and private credit funds alike.

But to be frank, my biggest concern here is not so much the quality of underwriting of these assets. The greatest risk is the timing. A promise to pay retirement benefits is inherently a long-term one. Plans for these long-dated commitments must be underwritten conservatively, of course, but in the end they must also be paid. And they must be paid with cash that is available on the date that the payment is due, not with hope that the asset will appreciate or that cash will become available at some later date. For disclosure, it is my firm's job to assess such liabilities and I worked at Apollo from 2008 to 2014.

The real risk is that income from the long-dated assets currently in the market will not be sufficient to service the debt needed to be put in place to support a retirement promise in the decades to come.

Another point that seems to be commonly held by the annuity industry is that illiquid assets will balance out against long-term illiquid policyholder liabilities and interest rate risk over time will be neutralised. I used to agree with this viewpoint but no longer. First, policyholder behaviour is not fixed. As annuities indexed to market indices have become more popular, the rates of people surrendering their annuities and or letting them lapse have become highly volatile. They can move in a sharp, non-linear fashion with "shock lapses" typically occurring after the end of periods when surrender charges apply. If there are enough early surrenders of these types of contracts in an insurer's portfolio of hard-to-price, illiquid assets, it could spur forced selling of those assets.

Recently, a number of the largest annuity issuers have begun to release more frequent marks to the net-asset-values of their private funds. While this is certainly a long overdue, positive step, reporting model-derived values is not the same as true price discovery. The manager's view of value is still embodied in the reported numbers.

The risks associated with the increasing presence of private capital in the life insurance sector have been known to regulators for several years. Since 2022 the US National Association of Insurance Commissioners has been cataloguing the following risks: 1) disclosure; 2) affiliated transactions; and 3) management compensation. The US Treasury department has begun to convene with state insurance regulators to look at how the roughly $1tn of private credit in the life insurance sector can be structured and managed in a way that does not expose policyholders to excessive risk of loss.

None of this is a call to panic. Nor is it a suggestion that these platforms are engaging in imprudent underwriting. Rather, my worry is far narrower and, I believe, far more significant: the illiquid private investments of asset managers have quietly emerged as the decisive competitive advantage in retirement finance.

At its core, life insurance exists to guarantee long-term promises will be paid when it is needed. All else — including returns — is secondary to that end. The critical issue of liquidity is a matter that should concern regulators, the directors of sector companies and the policyholders of life insurers. Better to address risks now before the industry faces a wave of policyholder surrenders that compels the sale of illiquid assets into weak markets.

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