

If insurance companies can secure member benefits while also generating attractive investment returns on their capital, why can't pension schemes – especially as, unlike insurance companies, pension schemes do not have to adhere to the strict matching requirements of Solvency II?

However, some pension schemes are finding it challenging to implement an insurance-like investment strategy in practice. We explore the reasons why – but more importantly, how trustees can overcome these challenges.

Investing like an insurance company

Insurance companies follow an approach like the one below, which is typically known as cashflow-driven investing (CDI).

Step 1: Buy and hold onto a portfolio of high-quality corporate bonds that will deliver payments in line with the insurer's pension obligations. When credit spreads are tight (as is currently the case) insurers will also often find other ways to match cashflows that still capture value, and then look to switch these into corporate bonds when spreads widen (more detail on this later).

Step 2: Invest in additional cashflow generating assets, like private credit to boost returns further.

Step 3: Use liability-driven investing (LDI) derivatives, like swaps, to top-up the interest rate and inflation hedge. The LDI strategy will consider the hedging already provided by the assets bought in Steps 1 and 2.

This insurance-like approach can also be beneficial for pension schemes because it gives trustees greater comfort that they will be able to meet their ongoing payment obligations, without having to sell assets at the wrong time. Investing in high-quality, contractual assets like investment grade (IG) corporate bonds can also reduce the chance of the pension scheme failing to achieve its long-term return objectives. Adding in LDI also protects the day-to-day funding position

DB pension schemes: Is investing like an insurer easier said than done?

The UK government recently published its highly anticipated Pension Schemes Bill, opening the door to more flexible treatment of defined benefit (DB) pension scheme surpluses. While buyout remains the gold standard for member security, many trustees and finance teams are now exploring if, and how, running-on their scheme could work for the benefit of its members and the sponsor

of the scheme from fluctuations in interest rates and inflation.

While the building blocks of CDI will be familiar to many trustees, they face several challenges when seeking to mirror this strategy in their pension scheme.

Challenge 1: Delivering high enough returns at the same time as matching

When implementing a CDI approach, pension schemes need to put aside enough assets to meet the collateralisation requirements of the derivatives in their LDI strategy, as well as to match their pension cashflow obligations.

Most pension schemes are only able to post cash or gilts as LDI collateral, which means they need to tie up a considerable proportion of their assets in these low yielding assets. Additionally, the credit spreads available on cashflow matching assets like corporate bonds are at historic low levels. These two factors mean that some pension schemes will struggle to generate high enough returns from their CDI strategy to make running-on worthwhile.

To offset the low yields available on their CDI portfolio, some schemes have retained a small proportion of their assets

in growth strategies (such as equities) that they hope will earn much higher returns – a so-called bar-bell approach. However, as relatively few asset classes are able to deliver these returns, this can lead to a very concentrated growth portfolio, with significant downside risk.

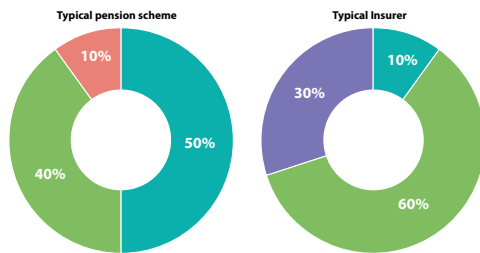
To overcome these challenges, insurers will usually implement LDI more flexibly than pension schemes. For example, they can typically post corporate bonds as LDI collateral, as well as cash and gilts, on attractive terms. This means that they can invest more of their assets in credit and less in gilts and cash to earn a higher yield on their CDI portfolio. This is particularly important for inflation hedging, for which there are fewer physical matching assets available that also deliver an attractive yield.

Insurers may also be able to use their balance sheet as a source of last-resort liquidity. Again, this can reduce the amount of cash they need to commit up front to support their LDI strategy.

An example pension scheme asset allocation and an example insurance company asset allocation are shown in the charts above. The insurance company can allocate more of its assets

Typical pension scheme and insurer asset allocation

LDI Corporate Bonds Growth Assets LDI, Gilts & Cash Diversified private credit



Source: M&G Investments, October 2025.

to corporate bonds and private credit than the pension scheme, which needs to hold more in gilts and cash to support its LDI strategy. The pension scheme has also retained a 10 per cent allocation to a concentrated growth asset strategy to enable it to achieve its long-term return objective. The insurance company has more assets available to achieve additional returns, so can construct a more balanced portfolio overall.

Insurers will also use their expertise, scale, and the strength of their bank counterparty relationships to access yield enhancing LDI strategies that may not be available to a typical pension scheme. For example, in the current tight spread environment insurance companies are using a combination of short-dated credit and leveraged gilt trades and/or par-par asset swaps to capture yield. Insurers may use these trades with the intention of switching into long-dated corporate bonds later on, when credit is priced more attractively¹.

Challenge 2: Accessing high quality private assets

Pension schemes can invest in a growing number of private assets; however, they are often at a competitive disadvantage when allocating to the highest quality investments.

In an increasingly crowded buyout market, insurance companies must source attractive assets to price new business competitively, and ensure they resource their teams accordingly. This is

especially true when spreads on public credit are tight.

When a new private asset comes to market, often only the very largest and most established investors, such as insurance companies, can participate. This means that pension schemes, which are usually making much smaller allocations, are unable to access these new opportunities.

Challenge 3: Bringing everything together in both normal and stressed markets

A CDI strategy needs to be able to fulfil a range of complex operational objectives at the same time: the timely delivery of cashflows to pay pensions, executing sophisticated derivative overlays, posting collateral and managing liquidity. These processes need to be robust in normal market conditions and during fast-moving crises like the 2022 gilts crisis.

Insurance companies have a long track-record of successfully managing these processes and experienced far fewer challenges than pension schemes during the gilts crisis. Most pension schemes with a CDI strategy will rightly seek to delegate some or all these functions to a third party.

A CDI plus liquidity solution that seeks to overcome challenges

To successfully invest like an insurer, trustees can appoint a CDI partner that has an insurance heritage. These can enable them to access the flexible LDI strategies, private markets expertise and scale, and operational resources of an insurance company, whilst retaining the benefits of a run-on solution.

M&G Investments works with trustees and their advisers to build a bespoke credit solution to match their pension scheme's cashflow profile. This can include corporate bonds and private credit if desired, and triggers can be used

to add longer-dated corporate bonds when spreads are more attractive.

Schemes are able to access the same highly flexible and efficient LDI strategies as our insurance company due to our wrapper that allows access to our balance sheet. The wrapper gives schemes the ability to use corporate bonds as LDI collateral and to 'borrow' liquidity from the insurance balance sheet in times of market stress.

With CDI plus liquidity, M&G Investments can also help pension schemes access many of the same private market strategies as the M&G plc group insurance company (Prudential) and, as these strategies are aligned with the Solvency II requirements of insurance companies, the solution can also act as a natural bridge to buyout.

If or when the pension scheme is ready to buyout, there is no obligation to transact with M&G Investments – the CDI plus liquidity solution is flexible and there are no additional costs for exiting the solution². However, M&G Investments will provide pricing for any CDI plus Liquidity client that wishes to consider buying out with us.

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If you would like to discuss any of the topics in this paper please contact the Endgame Solutions team.



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¹ With CDI we hope to hold corporate bonds until they mature, so it can make sense to delay buying longer dated bonds until credit spreads are more attractive. The values of longer dated corporate bonds are also more sensitive to widening spreads than shorter dated bonds. This can be an extra consideration for pension schemes who are concerned about the day-to-day volatility of their assets compared to their liabilities (particularly if their liabilities are discounted on a gilts rather than corporate bond basis). ² Selling the underlying assets may incur transaction costs; however, M&G does not charge any additional fees for exiting the CDI plus Liquidity solution and there is no minimum investment period. This Financial Promotion is issued by M&G Investment Management Limited, registered in England and Wales under number 936683, registered office 10 Fenchurch Avenue, London EC3M 5AG. M&G Investment Management Limited is authorised and regulated by the Financial Conduct Authority.