White Paper

CLOs unlocked: How European insurers' fixed income rules are being rewritten

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STATE STREET INVESTMENT MANAGEMENT

Collateralised loan obligation exposures may move to the mainstream of European insurers' fixed income portfolios, following regulatory reform.

Securitised credit, particularly collateralised loan obligations (CLOs), have occupied a marginal position in European insurance portfolios for some years. Despite offering attractive yields, diversification benefits and a strong historical track record, allocations to any securitised instrument have remained limited, largely due to unfavourable regulatory capital treatment under Solvency II, the European Union's risk-based regulatory framework for insurance and reinsurance companies, which sets rules on capital adequacy and risk management.

This contrasts with other markets, most notably the United States, where insurers have embraced securitised assets as a core component of their fixed income allocations. The divergence highlights not a lack of investment merit, but the powerful influence of regulatory frameworks in shaping portfolio construction decisions.

But the latest Solvency II reforms may signal a turning point. European policymakers are seeking to address a long-recognised mismatch between regulatory charges and underlying risk by recalibrating capital requirements for securitisations, particularly for high-quality and senior tranches.

As a result, insurers are increasingly re-evaluating the role that securitised credit can play within their portfolios as a result. The revised framework reshapes the investment case for securitised assets, the implications for portfolio construction, and how CLOs may move from niche allocation to strategic portfolio component in a capital-efficient and operationally practical way.

Solvency II reform and securitised credit: What it means for European insurers

Earlier iterations of Solvency II helped keep securitised credit on the fringe of most European insurance portfolios. For insurers operating under Solvency II's standard formula, the regulator's prescribed methodology for calculating solvency capital requirements (SCR), securitised assets typically account for less than 1% of total invested assets.[1] The reasons for this persistent underinvestment are not entirely clear, but unfavourable capital treatment, which has made the asset class inefficient from a return-on-capital perspective, has likely been a factor.

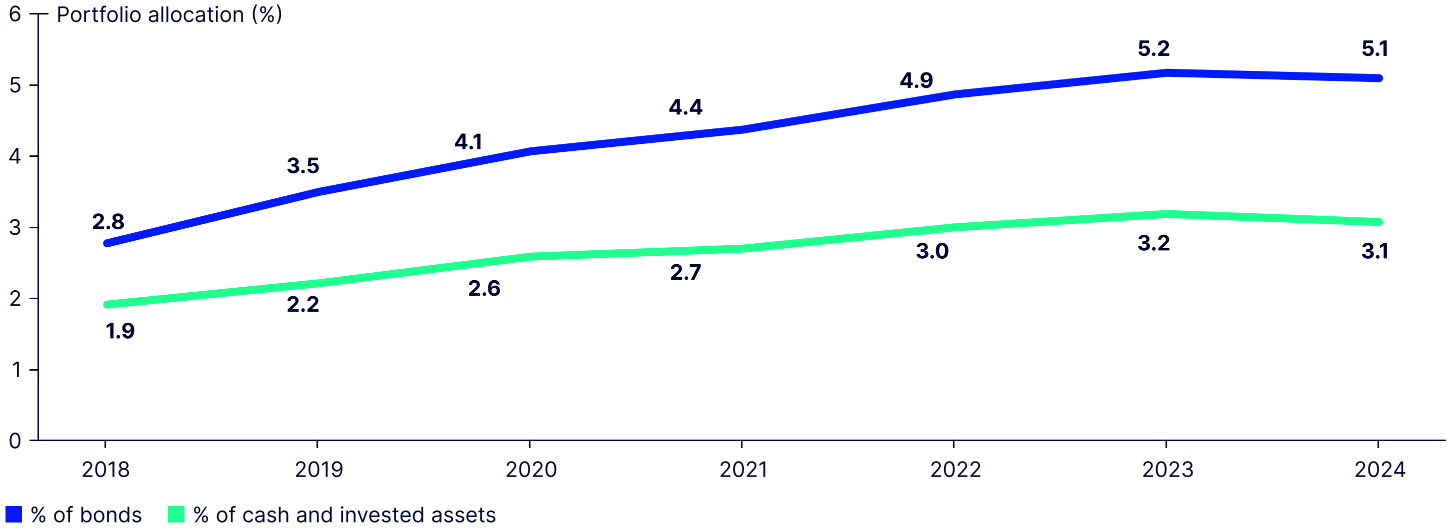
When Solvency II was implemented in 2016, capital charges for securitisations were set conservatively. In practice, this meant that senior securitised tranches often attracted materially higher capital requirements than corporate bonds with similar ratings, duration, and loss experience.

As a result, their prospective returns on regulatory capital for securitisation investments became very low, and European insurers largely withdrew from the market.

The introduction of Simple, Transparent and Standardised (STS) securitisations in 2019 was intended to address some of the structural and prudential concerns around the asset class, but in practice it has not impacted insurers' investment behaviour or overall allocations.

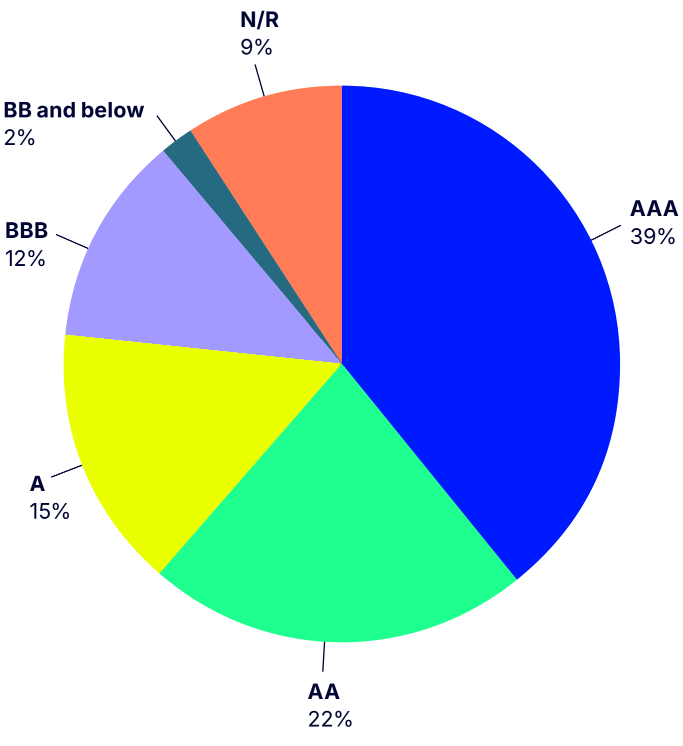
In the US, securitised credit represents a significantly larger share of insurance companies' allocations. Approximately 3% of cash and invested assets were invested in collateralised loan obligations (CLOs) alone as at year-end 2024.[2] Importantly, this exposure is primarily to senior, high-quality positions: around 80% of US insurers' CLO holdings are investment grade (IG) or higher (i.e. rated at least BBB). Approximately 40% are rated AAA.

Figure 1: US insurers' CLO investments as a percentage of total
% of bonds vs. % of cash and invested assets



Source: National Association of Insurance Commissioners: Capital Markets Special Report CLO YE 2024.

Figure 2: US insurers' CLO credit quality



Source: National Association of Insurance Commissioners: Capital Markets Special Report CLO YE 2024.

As a result of the Solvency II capital treatment, insurers' prospective returns on regulatory capital for securitisation investments became very low, and they largely withdrew from the market. Previously, insurers typically accounted for about 15% of order books on new securitization issuances, but their involvement in the primary market is now minimal.[3]

This may now change. The latest Solvency II reforms are widely seen as marking a meaningful shift. With the adoption of Commission Delegated Regulation (EU) 2026/269 from January 2027, European policymakers have recalibrated the capital framework for securitisations, aiming to better reflect their underlying risk and to encourage long-term investment where appropriate. In addition, insurers will be able to play a more active role in securitisation markets by facilitating the transfer of risk outside the banking sector.[4]

Insurers that use internal models, typically large composite (re)insurers, have remained more active in securitised credit than those relying on the standard formula. By leveraging internal modelling capabilities, these firms have been able to capture the underlying risk profile of these instruments with greater precision, incorporating granular assumptions around tranche structure, cashflow dynamics and credit performance. This has enabled them to justify more proportionate capital charges and maintain selective exposure to high-quality securitisations.

By contrast, most European insurers rely on the Standard Formula, the regulator's prescribed methodology for calculating SCR. For these insurers, capital treatment has historically been a more significant constraint on allocations to securitised assets. In this context, the latest reform represents an important development for standard formula insurers. It strengthens the investment case for an asset class that can support portfolio diversification and improve capital efficiency without weakening regulatory safeguards. In this context, the recalibration is less a step-change for internal model firms and more a recognition of existing practice, while meaningfully narrowing the gap with standard formula insurers who can now re-engage under a more balanced and transparent capital framework.

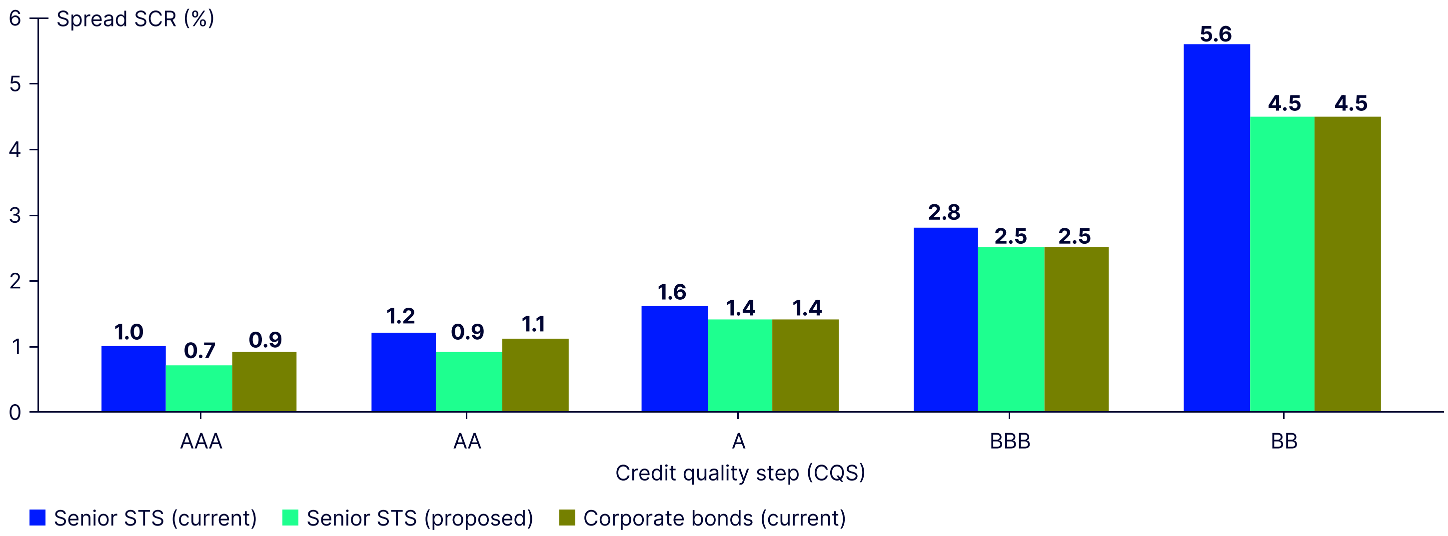
The Solvency II review explicitly acknowledges that capital requirements had become misaligned with economic risk, and that this miscalibration was discouraging productive long-term investment. For example, for non-simple, transparent and standardised (STS) securitisations, current regulation does not distinguish between senior and non-senior tranches. This lack of risk sensitivity results in an overestimation of spread risk, particularly for investments in the highest-quality tranches. The reform seeks to address that imbalance while maintaining policyholder protection as the central objective.

What has changed

The updated delegated regulation introduces targeted changes to how spread risk is calculated for securitised assets under the standard formula.

1 Lower capital charges for certain senior and non-senior STS securitisations, reflecting their strong credit enhancement and historically low volatility. For senior and non-senior STS securitisations capital charges are reduced between 11–30% depending on the credit quality of the asset, with the largest reductions applying to the highest rated assets. Capital charges for senior-STS securitisation will be aligned more closely to those applicable to corporate bonds.

Figure 3: Senior STS vs. Corporate Bond Spread Risk SCR
Current vs. proposed by credit quality step (1-year spread duration)



Source: European Commission, (July 2025): Commission seeks feedback on the review of the Solvency II Delegated Regulation.

Figure 4: Spread SCR for non-STS securitisations by credit quality step (CQS) and spread duration (current vs. new)

Spread risk SCR for non-STS (%)		Senior		Non-senior	
		1 y	5 y	1 y	5 y
CQS 0 (AAA)	Current	12.5	62.5	12.5	62.5
	New	**2.7**	**13.5**	**7.4**	**37.0**
	Change (p.p.)	-10	-49	-5	-26
CQS 1 (AA)	Current	13.4	67.0	13.4	67.0
	New	**3.3**	**16.5**	**9.0**	**45.0**
	Change	-10	-51	-4	-22
CQS 2 (A)	Current	16.6	83.0	16.6	83.0
	New	**4.4**	**22.0**	**12.0**	**60.0**
	Change	-12	-61	-5	-23
CQS 3 (BBB)	Current	19.7	98.5	19.7	98.5
	New	**7.5**	**37.5**	**18.8**	**94.0**
	Change	-12	-61	-1	-5
CQS 4 (BB)	Current	82.0	100.0	82.0	100.0
	New	**14.3**	**71.5**	**38.9**	**100.0**
	Change	-68	-29	-43	0

Source: European Commission (July 2025): Commission seeks feedback on the review of the Solvency II Delegated Regulation. **Performance data quoted represents past performance. Past performance does not guarantee future results.**

2 An expansion of the current category of non-STS securitisations and introduction of distinct capital charges for senior and non-senior tranches. In particular, the revised framework introduces lower risk factors for senior non-STS securitisations, bringing the capital treatment of senior tranches more closely in line with their underlying risk profile and narrowing the gap with banking capital requirements. In practice, this means:

- Lower capital charges for certain senior securitisations, reflecting their substantial credit enhancement and historically low volatility
- More risk-sensitive differentiation, based on rating quality and duration, reducing cliff effects within the capital framework
- A clear policy indication that high-quality securitisations can play a role in insurers' long-term investment strategies

The reform does not represent a blanket relaxation. Capital requirements remain higher for more complex or subordinated tranches, and insurers are still expected to apply robust due diligence and risk management.

Most of the changes are scheduled to take effect in January 2027.

What has not changed

While capital treatment is becoming more proportionate, the underlying complexity of securitisations remains unchanged.

The reform does not reduce the need for robust investment discipline: insurers must continue to assess structural features in detail, including tranche positioning, cashflow waterfalls, and embedded trigger mechanisms.

Equally, comprehensive stress testing, scenario analysis and ongoing monitoring of the underlying collateral remain essential. Successful implementation will depend on integrating securitised exposures within a broader asset-liability management and solvency framework, ensuring they are considered as part of the overall balance sheet strategy, rather than as a standalone allocation.

Portfolio construction: CLOs move from niche allocation to strategic portfolio component

These changes may enhance the appeal of CLOs within European insurers allocations. CLOs should be viewed as a complementary allocation within a diversified strategy—not a replacement for traditional fixed income. Their combination of yield potential, diversification benefits, and capital efficiency enables them to sit alongside existing exposures to IG credit, private debt, and other spread assets.

From a portfolio perspective, senior CLO securitisations may help insurers:

1 Access granular, well-structured pools of risk

CLOs are backed primarily by loans to non-IG borrowers. However, risk reduction in the securitised structure takes several forms:

- CLO collateral pools are typically broad and well diversified. A CLO may contain exposure to more than 175 borrowers across multiple industries, offering greater resilience to issuer-specific or sector-specific shocks. The loans are often senior secured, which should support recovery rates in the event of an issuer default.
- CLO funds are actively managed and provide a high degree of transparency. Managers can trade underlying loans, which can help mitigate the impact of deteriorating credit fundamentals.
- The tranche structure of CLOs enables investors to focus on the most senior AAA-rated securities. These tranches benefit from substantial subordination, meaning losses would need to exceed the level of subordinated capital before principal losses would be experienced by AAA investors.
- The track record for CLOs has been resilient, with no European CLO rated single-A or above having defaulted since the inception of CLOs.[5]

2 Diversify sources of spread

Although many of the factors that impact corporate credit spreads also affect CLO spreads, their sensitivity to these factors can differ (Figure 5). There has been more volatility in Euro IG spreads than in CLO spreads since 2023. While IG credit spreads remain at historically very compressed levels, the CLO discount margin is comfortably above the tights seen in 2019. Moreover, discount margin moves have been relatively contained in 2026 year-to-date versus broader credit spreads. The regression beta suggests discount margin widening of less than 50% of the moves seen for IG.

Figure 5: EUR AAA CLO discount margin vs. Euro IG spreads

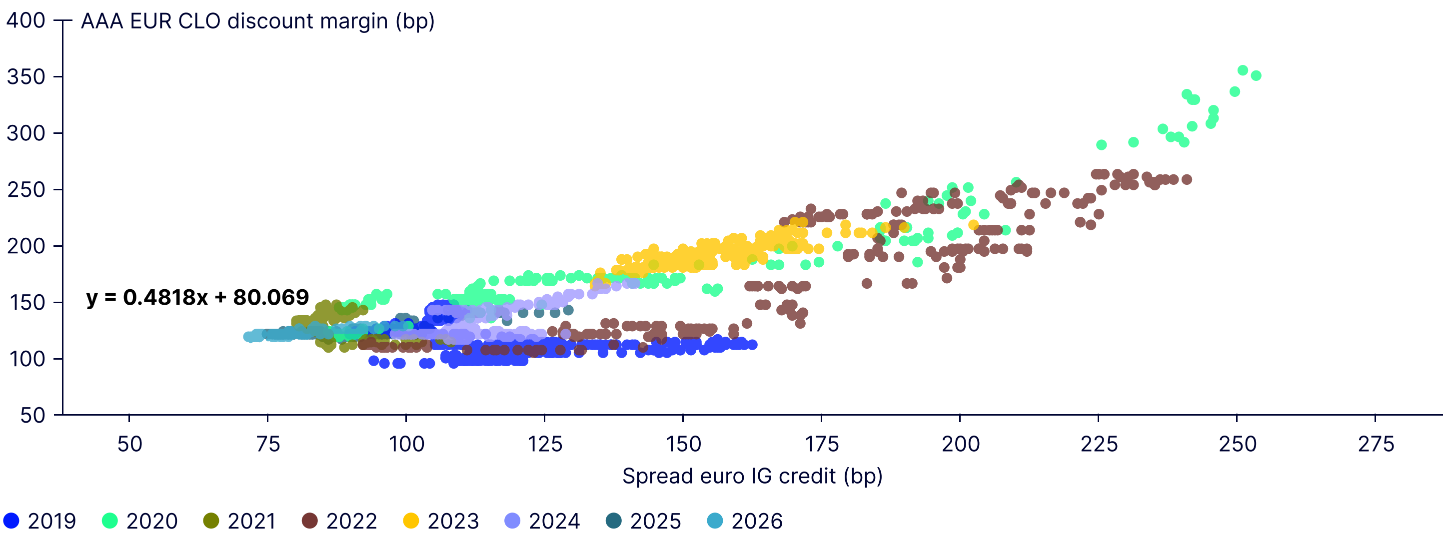


Chart shows the discount margin on the J.P. Morgan Euro CLOIE AAA Index versus the index option-adjusted spread to Treasurys of the Bloomberg Euro Corporates Index. Source: State Street Investment Management, Bloomberg Finance, L.P., as at 31 July 2026. **Performance data quoted represents past performance. Past performance does not guarantee future results.**

3 Enhance capital efficiency within existing solvency limits.

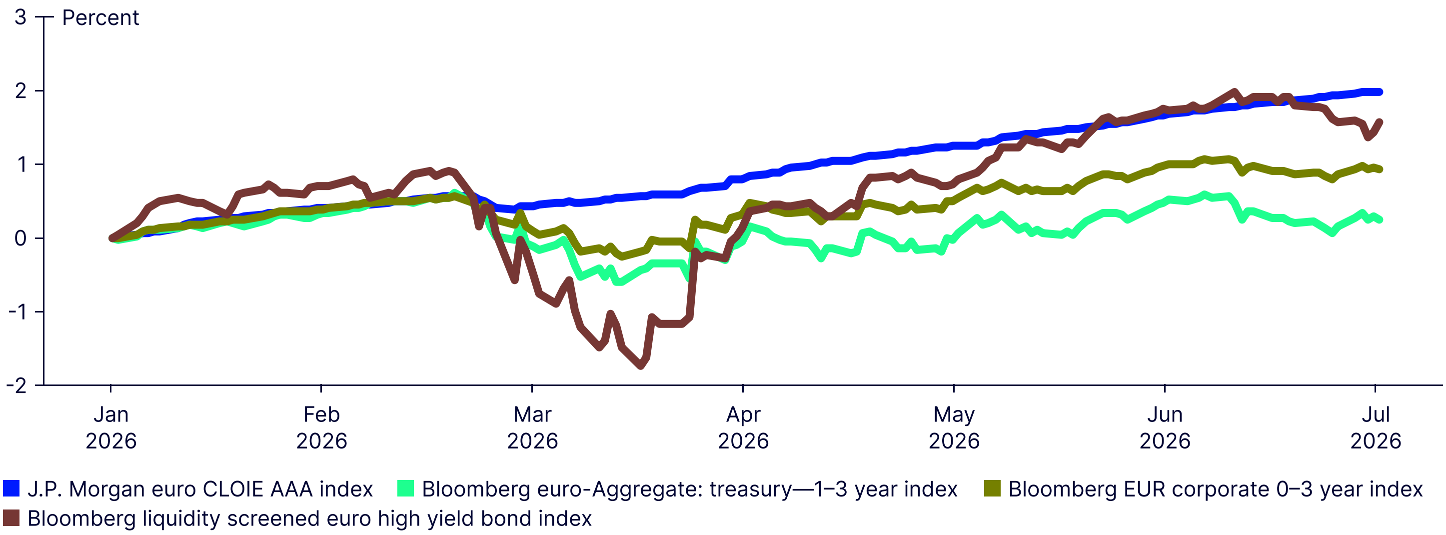
- The yield-to-worst on a Euro AAA CLO has historically been similar to or even above, an all-maturities IG strategy.[6] Under the revised framework, the SCR for AAA-rated securities will be lower than that associated with a broad investment grade allocation, which includes A-/BBB+ securities, supporting more efficient use of capital
- In addition, the duration on the CLO tranche will be around ¼ year against around 4.5 years for an all-maturities fund. This may allow managers to improve their portfolio credit quality and reduce interest rate sensitivity while improving their overall portfolio credit quality and lowering duration risk[7]

These features are especially relevant where balance sheet flexibility is limited, and capital efficiency is a binding constraint.

4 Support long-term investment objectives

The securitisation reforms should be viewed in the context of the broader Solvency II review, which aim to encourage long-term investment and reduce excessive conservatism across the framework. Within that setting, securitised credit can support stable cashflow profiles: Low correlations to traditional fixed income securities can assist with portfolio diversification. The short duration and floating rate nature of CLOs may help reduce sensitivity to changes in interest rate expectations. Coupled with cross sector diversification, this has contributed to a relatively low correlation of 64% to Euro corporates and a very low 36% to Euro Aggregate over the past eight years.[8] As Figure 6 illustrates, Euro AAA CLOs demonstrated relative resilience at the start of the recent US-Iran conflict, outperforming several short-duration fixed income strategies.

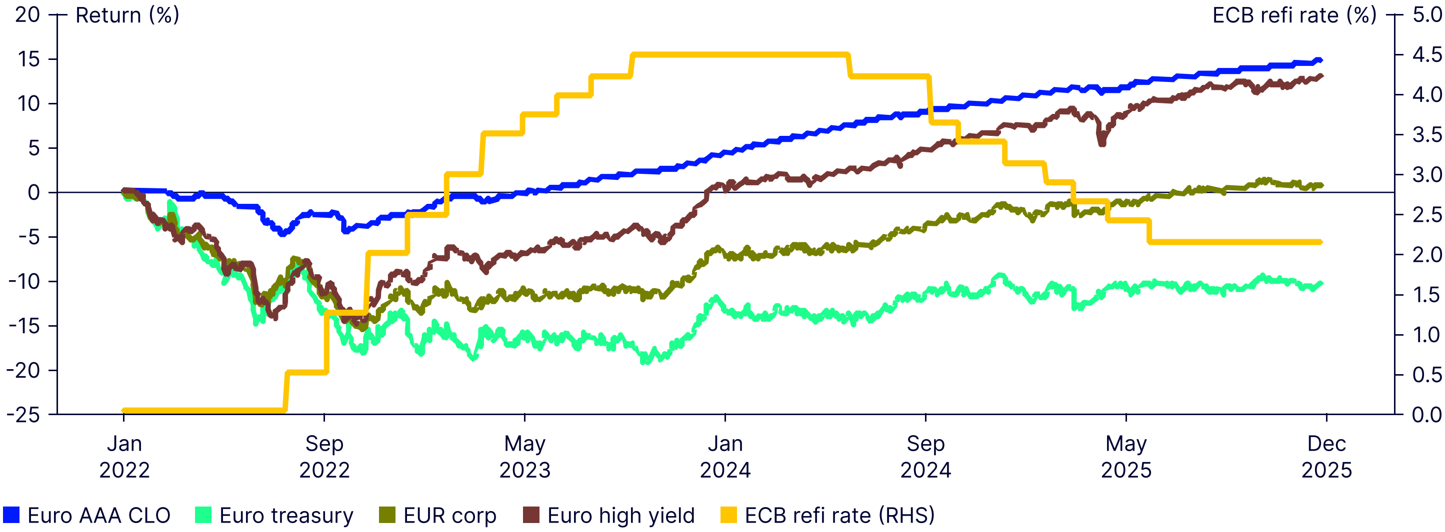
Figure 6: Euro AAA CLO drawdowns were limited versus other short duration strategies



Cumulative total index returns in 2026 from 31 December 2025. Source: State Street Investment Management, Bloomberg Finance, L.P., as at 31 July 2026. **Performance data quoted represents past performance. Past performance does not guarantee future results.**

There is also evidence that CLOs can help smooth returns across a policy cycle. Chart 6 shows cumulative returns for various euro-denominated fixed income strategies during the 2022-2025 European Central Bank rate cycle. Measured from six months before the first rate rise, CLO returns were higher than the other strategies, including high yield (Figure 7). This can be attributed in part to the defensive nature of CLOs, which helped to limit losses at the early stages of the tightening cycle.

Figure 7: Euro AAA CLOs performed strongly over the latest ECB policy cycle

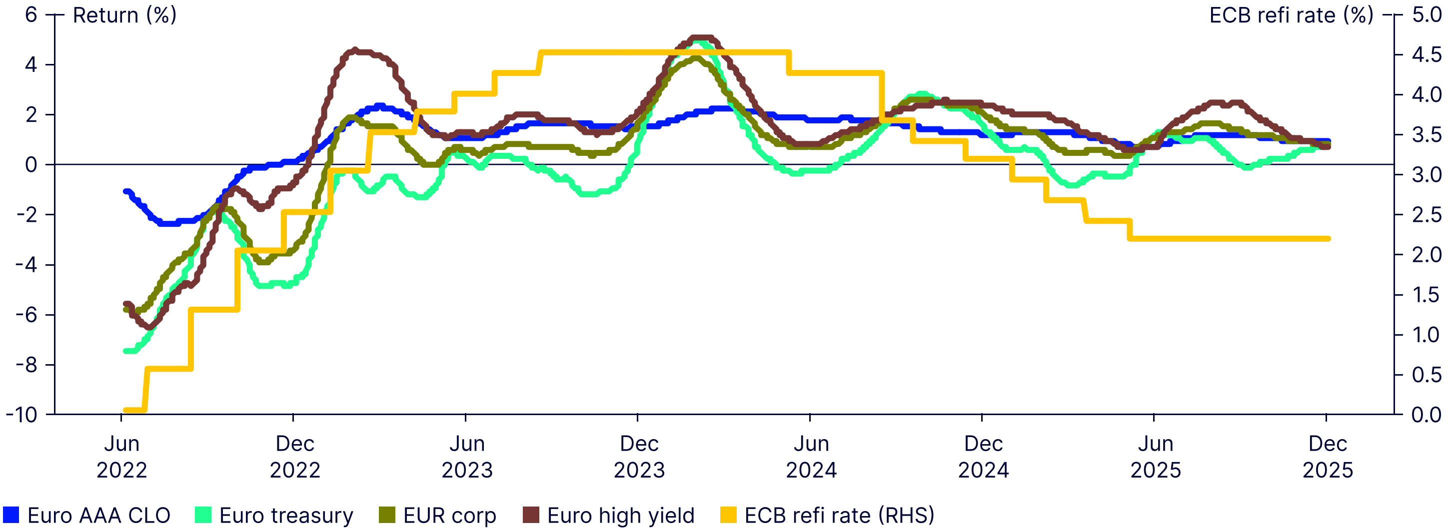


Cumulative total index returns over the 2022 to 2025 period from 31 December 2021. Source: State Street Investment Management, Bloomberg Finance, L.P., as at 30 April 2026. **Performance data quoted represents past performance. Past performance does not guarantee future results.**

Limited drawdowns helped to promote portfolio stability at the start of the cycle but the absence of interest rate duration did not prevent CLOs from generating competitive returns over the remainder of the cycle. High coupon income sustained performance. Consider the 3-month/3-month total return for the same strategies (Figure 8). Several observations stand out:

- Early in the tightening cycle, CLOs offered a clear advantage over strategies with greater duration exposure. Notably, CLO returns exceeded other strategies even though central bank rates were close to zero and coupon levels were low
- As the tightening cycle matured, high yield returns outperformed CLOs, as fears over a growth slowdown receded. However, as rates peaked, returns converged
- At the turn in the cycle, when the market began pricing in lower future policy rates, duration-sensitive strategies outperformed CLOs
- CLO returns were higher and more stable than those of other strategies at the start of the rate-cut cycle. From the midpoint onwards, high yield was the strongest performer, and euro government bonds underperformed

Figure 8: 3-month on 3-month rolling returns over the last ECB policy cycle

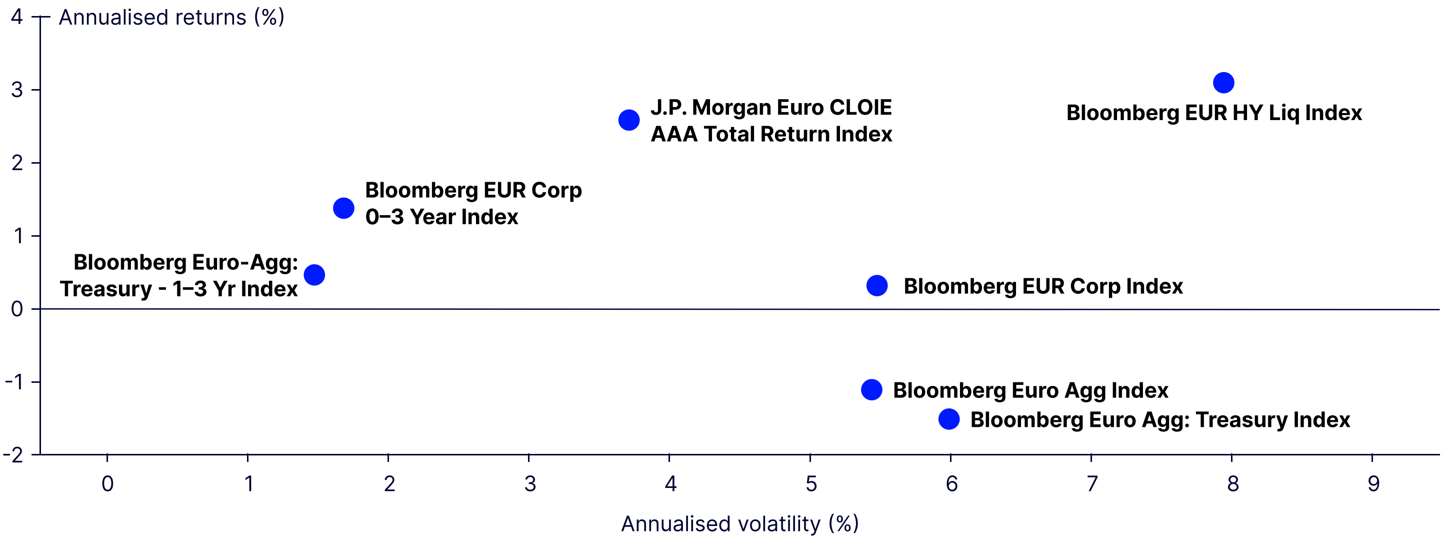


3-month on 3-month index returns. Source: State Street Investment Management, Bloomberg Finance L.P. as at 30 April 2026. **Performance data quoted represents past performance. Past performance does not guarantee future results.**

Weak returns from duration-sensitive strategies have been a feature of this cycle but the 3-month on 3-month rolling returns also highlight the stability of CLO performance. Limited drawdowns and low volatility reflect the contribution of coupon income to overall returns.

Consider the seven-year annualised index returns against volatility for a range of euro-denominated index strategies (Figure 9). Over this period, which includes the Covid-related market disruptions, the J.P. Morgan Euro CLOIE AAA Index exhibited more volatility than short-duration strategies, which would have been considered safe haven trades, but 62% of the volatility associated with the Euro Aggregate Treasury index and less than half of the volatility of euro-denominated high yield.[9] Annualised total returns exceeded IG strategies and almost reached 75% of those delivered by euro high yield.

Figure 9: Seven-year annualised returns versus volatility



Annualised index returns versus annualised volatility over the past seven years. Source: State Street Investment Management, Bloomberg Finance, L.P., as at 31 July 2026. **Performance data quoted represents past performance. Past performance does not guarantee future results.**

Improving liquidity profile

An allocation to CLOs can also improve the liquidity of portfolios. Using ETFs in fund liquidity sleeves is already a well-established practice for liquidity management. Where a portfolio experiences a significant cash requirement, the ETF holdings can be sold down to accommodate the funding needs. This leaves the core portfolio holdings unaffected, which can be especially valuable where the portfolio is structured to match against liabilities.

A CLO allocation can also be used more directly in the cash portion of a portfolio. Despite its AAA-rating, CLOs are not a direct substitute for cash holdings but the high levels of liquidity mean that a portion of the liquidity allocation can be invested in CLOs. US insurers hold around 3% of their cash and investment holdings in CLOs (Figure 2). Given yields on AAA-rated CLOs are typically more than 100 basis points above three-month Euribor rates, they may materially improve returns over cash.[w] The growth of CLO ETFs in Europe, coupled with increased adoption of CLOs by insurers, may support liquidity in the underlying asset class.

CLOs can become mainstream for insurers

Solvency II reform represents an important development for securitised credit within European insurance portfolios. By aligning capital charges more closely to underlying risk, it removes a long-standing barrier, and enables insurers to reassess the asset class on a more consistent footing with other comparable spread assets.

This may strengthen the case for senior securitisations, particularly high-quality CLOs, as a complementary allocation that can enhance diversification, improve capital efficiency, and support resilient income generation.

Accessing this opportunity may require flexibility in implementation. A range of investment approaches, including dedicated mandates, pooled funds and ETF structures, can help insurers tailor exposures to their specific balance sheet, liquidity, and governance requirements. ETFs, for example, offer advantages in terms of transparency, liquidity, and ease of access.

Ultimately, the reforms do not change the need for discipline, but they do broaden the available opportunity set. For insurers, the focus shifts from regulatory constraint to implementation considerations, including how securitised credit can be incorporated within a well-diversified, capital-efficient portfolio aligned with long-term objectives.

Learn more about CLO ETFs.

Endnotes

1 EIOPA: Insurance regulatory framework for securitisation (February 2024).

2 National Association of Insurance Commissioners: Capital Markets Special Report CLO YE 2024.

3 S&P Global: Will solvency II changes unlock Securitisation for EU insurers?

4 European Commission (July 2025): Commission seeks feedback on the review of the Solvency II Delegated Regulation.

5 Blackstone, as at 31 May 2026.

6 State Street Investment Management, as at 30 July 2026. **Performance data quoted represents past performance. Past performance does not guarantee future results.**

7 State Street Investment Management, J.P. Morgan, Bloomberg Finance, L.P., as at 31 May 2026. CLOs are floating rate with quarterly resets, which is why the interest rate duration is short. There is also credit spread duration which is not referenced here.

8 The J.P. Morgan Euro CLOIE AAA Index has just a 36.1% correlation to the Bloomberg Euro Aggregate total return Index and 64.3% to the Bloomberg Euro Corporate index based off monthly data since Jan 2018. Source: State Street Investment Management, as at 29 May 2026. **Performance data quoted represents past performance. Past performance does not guarantee future results.**

9 Source: State Street Investment Management, Bloomberg Finance, L.P., as at 31 July 2026.

10 The yield on the J.P. Morgan Euro CLOIE AAA Index was 110bps above 3-month Euribor. Source: Bloomberg Finance, L.P., as at 29 May 2026. **Performance data quoted represents past performance. Past performance does not guarantee future results.**

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* This figure is presented as of June 30, 2026 and includes ETF AUM of $2,203.98 billion USD of which approximately $156.81 billion USD in gold assets with respect to SPDR products for which State Street Global Advisors Funds Distributors, LLC (SSGA FD) acts solely as the marketing agent. SSGA FD and State Street Investment Management are affiliated. Please note all AUM is unaudited.

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CLO Debt Securities carry certain structural risks including potential subordination to the other tranches of debt in the same capital structure, volatility of underlying collateral values, and potential for principal loss of the underlying assets in excess of the equity valuation. CLOs issue classes or "tranches" of securities that vary in risk and yield. Losses caused by defaults on underlying assets are borne first by the holders of subordinate tranches.

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